

**AGENDA — July 25, 2000 Business Taxes Committee Meeting**  
**Proposed Regulatory Changes to Clarify the Application of Tax to Sales**  
**Requiring a Seller's Permit (Regulation 1595)**

<b>Action 1 — Consent Item(s)</b>  Proposed amendments to Regulation 1595, <i>Occasional Sales – Sale of Business – Business Reorganization</i>	Adopt proposed amendments to Regulation 1595 as proposed by staff. Industry has raised no objections to these amendments.
<b>Action 2 — Authorization to Publish</b>	Direct the publication of proposed amendments to Regulation 1595 as adopted in the above action.  Operative Date:   None Implementation:   Upon OAL approval

**AGENDA — July 25, 2000 Business Taxes Committee Meeting**  
***Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a Seller's Permit (Regulation 1595)***

Action Item	Staff's Proposed Regulatory Language
<p><b>Action 1 — Consent Item(s)</b></p> <p>Proposed amendments to Regulation 1595, <i>Occasional Sales of a Business – Business Reorganization</i></p>	<p>Regulation 1595. Occasional Sales--Sale of a Business--Business Reorganization.</p> <p>(a) ACTIVITIES REQUIRING SELLER'S PERMIT.</p> <p>(1) GENERAL. Tax applies to all retail sales of tangible personal property including capital assets whether sold in one transaction or in a series of sales, held or used by the seller in the course of an activity or activities for which a seller's permit or permits is required or would be required if the activity or activities were conducted in this state. See subdivision (e) below for special rules regarding sales of property by producers of hay.</p> <p>Generally, a person who makes three or more sales for substantial amounts in a period of 12 months is required to hold a seller's permit regardless of whether the sales are at retail or are for resale. Each sale of the person during the 12 month period is included in determining whether that person is required to hold a permit, or would be required to hold a permit if the activities were conducted entirely inside this state. Thus, a sale occurring outside California, whether at retail or for resale, is included, even though it would not be subject to California sales tax. A person who makes a substantial number of sales for relatively small amounts is also required to hold a seller's permit.</p> <p>Tax does not apply to a sale of property held or used in the course of an activity not requiring the holding of a seller's permit unless the sale is one of a series of sales sufficient in number, scope and character to constitute an activity for which the seller is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state. If tangible personal property is leased under a lease which is a "sale" as defined in Revenue and Taxation Code Section 6006 or a "purchase" as defined in Revenue and Taxation Code Section 6010, tax applies to the lease as provided in Regulation 1660 (18 CCR 1660), and the lessor must hold a seller's permit as provided in Regulation 1699 (18 CCR 1699). The lessor is not making an occasional sale since the lessor is making a "continuing sale" and is thereby holding the leased property in an activity requiring the holding of a seller's permit. As such, the lessor's sale of the leased property at the end of the lease term is likewise not an occasional sale.</p>

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	<p>(2) PROPERTY HELD OR USED IN AN ACTIVITY, OR ACTIVITIES REQUIRING THE HOLDING OF A SELLER'S PERMIT. A seller's permit is required of a person engaged in the business of selling tangible personal property. An activity requiring the holding of that permit includes, but is not limited to, the acquisition and sale of tangible personal property, whether the person's sales are all at retail, all for resale, or include both sales at retail and sales for resale.</p> <p>Acquisition includes the obtaining of the property in any manner whatsoever. For example, raw materials may be purchased or may be obtained by extraction from the earth, air or waters of the earth. These may be sold in raw form or processed or manufactured into other raw materials, component parts or finished items which are sold. Each of these activities is an activity which is so related to the sale of tangible personal property, that it is part of the activity requiring the holding of a seller's permit.</p> <p>(3) SEPARATE BUSINESSES. A person engaged in an activity or activities requiring the holding of a seller's permit or permits may also be engaged in entirely separate endeavors which do not require the holding of a seller's permit or permits. Tax applies to the sale of tangible personal property held or used in the course of an activity requiring the holding of a seller's permit. Tax does not apply to the sale of property held or used by the seller in the non-selling endeavors which do not require the holding of a permit unless that sale is itself one of a series of sales requiring the holding of a seller's permit. For example, a person may own a hardware store at one location and a real estate brokerage business at another location, with no relationship between the two activities except that of common ownership. Under these circumstances, a sale of furniture used in the brokerage business would not be a sale of property held or used in an activity requiring the holding of a seller's permit unless it was one of a series of sales of the property of the brokerage business. A sale of tangible personal property held or used in the hardware business would be a sale of property held or used in an activity requiring the holding of a seller's permit.</p> <p>(4) SERIES OF SALES REQUIRING THE HOLDING OF A SELLER'S PERMIT. <del>When a A</del> person not otherwise engaged in an activity requiring the holding of a seller's permit <u>may make</u> <del>makes</del> a series of sales sufficient in number, scope and character to require the holding of a seller's permit, <del>the gross receipts from all of such sales are subject to tax.</del> <u>The sale in that series of sales, and subsequent sales, during any 12 month period which resulted in the requirement to hold a permit are subject to tax, unless otherwise exempt.</u></p>

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	<p>(A) Number.</p> <p>1. Generally the minimum number of sales to require the holding of a seller's permit by a person not otherwise engaged in a selling activity is three within any 12 month period.</p> <p>2. When calculating the minimum number of sales which requires a person to hold a seller's permit, the following types of sales are excluded:</p> <ul style="list-style-type: none"> <li>a. Sales made by an auctioneer on behalf of the person. In such transactions, the auctioneer is the retailer liable for tax.</li> <li>b. Sales through claiming races of horses owned by the person. In such transactions, the racing association is the retailer liable for tax.</li> <li>c. Sales of vehicles, mobilehomes, commercial coaches, vessels, or aircraft which are exempted from sales tax by Revenue and Taxation Code Sections 6282 and 6283.</li> <li>d. A trade-in made by the person which is incidental to a nonselling activity of the person.</li> </ul> <p>(B) Scope. The extent of the sales measured by their frequency or dollar volume.</p> <p>(C) Character. This relates to the similarity in type and value giving effect to the taxpayer's operations. For example, a processor of food products for human consumption is not required to hold a seller's permit for the processing and sale of food products. Sales of used lug boxes, obsolete or used machinery, food handling and similar items are of a character that three or more sales of sufficient scope will require the processor to hold a seller's permit for this selling activity.</p> <p>(5) EXAMPLES APPLYING THE ABOVE PRINCIPLES.</p> <p>(A) Service enterprises which make some incidental sales.</p> <p>1. Operators of service enterprises such as hospitals, hotels, theaters, schools, laundromats, car washes, transportation companies, and trucking companies may make some sales incidental to their primary service business. A hospital may operate a pharmacy and cafeteria as an adjunct to the hospital. A hotel may operate a restaurant and a bar. A theater may sell popcorn to patrons. A school may operate a cafeteria and bookstore. A laundromat may sell soap to its customers.</p>

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	<p>If any of these businesses were sold, tax would apply only to the gross receipts from the tangible personal property held or used in the selling activity.</p> <p>2. If, in any 12 month period, the operator of the service enterprise makes more than two sales in substantial amounts of tangible personal property used in the service enterprise, <del>none of the sales qualify as an occasional sale</del> <u>the first two sales are exempt occasional sales, but the operator is required to hold a permit for the third and subsequent sales during any 12 month period. The gross receipts from the third and subsequent sales during any such 12 month period are subject to tax, unless otherwise exempt. For example, if one sale is a sale in interstate commerce, the gross receipts from that sale would be exempt; however, the gross receipts from the other sales would be taxable. If one of the sales is a sale of the business, sales tax applies to the gross receipts from the retail sale of the tangible personal property located in California and use tax applies to the sales price of property purchased for use in California and used in this state. For example, the only sales that a service enterprise made were the following sales (each of which was "substantial" for purposes of this regulation) of tangible personal property used in the service enterprise:</u></p> <table data-bbox="905 906 1520 1240"> <tr><td>a. February 23, 1996</td><td>Occasional sale</td></tr> <tr><td>b. August 16, 1996</td><td>Occasional sale</td></tr> <tr><td>c. January 8, 1997</td><td>Not occasional sale</td></tr> <tr><td>d. February 8, 1997</td><td>Not occasional sale</td></tr> <tr><td>e. January 27, 1998</td><td>Occasional sale</td></tr> <tr><td>f. February 3, 1998</td><td>Not occasional sale</td></tr> <tr><td>g. August 11, 1999</td><td>Occasional sale</td></tr> <tr><td>h. December 12, 1999</td><td>Occasional sale</td></tr> <tr><td>i. September 8, 2000</td><td>Occasional sale</td></tr> <tr><td>j. December 9, 2000</td><td>Not occasional sale</td></tr> </table> <p><u>Sales a. and b. are occasional sales since since they were the first two sales made by the service enterprise.</u></p> <p><u>Sales c. and d. are not occasional sales since they were the third and fourth sales in the series of sales commencing on February 23, 1996, which was less than 12 months prior to these sales.</u></p>	a. February 23, 1996	Occasional sale	b. August 16, 1996	Occasional sale	c. January 8, 1997	Not occasional sale	d. February 8, 1997	Not occasional sale	e. January 27, 1998	Occasional sale	f. February 3, 1998	Not occasional sale	g. August 11, 1999	Occasional sale	h. December 12, 1999	Occasional sale	i. September 8, 2000	Occasional sale	j. December 9, 2000	Not occasional sale
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	<p><u>Sale e. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on February 8, 1997. The January 8, 1997 sale is not relevant since it occurred more than 12 months prior to sale e.</u></p> <p><u>Sale f. is not an occasional sale since it was the third sale in the series of sales commencing on February 8, 1997, which was less than 12 months prior to this sale.</u></p> <p><u>Sale g. is an occasional sale since the service enterprise made no other sales in the prior 12 months.</u></p> <p><u>Sale h. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on August 11, 1999.</u></p> <p><u>Sale i. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on December 12, 1999.</u></p> <p><u>Sale j. is not an occasional sale since it was the third sale in the series of sales commencing within the prior 12 months, on December 12, 1999.</u></p> <p>(B) Other businesses.</p> <p>1. Tax applies to the sales of assets of a business which is not essentially a service enterprise. Examples of this are sales of grocery stores and liquor stores making both exempt sales of food products for human consumption and taxable sales of other tangible personal property, service stations which sell gasoline, oil and similar items and which also perform automotive repairs and lubrication services, and computer stores which also provide training in the use of computers and repairs for computer products.</p> <p>2. Where a service enterprise and a sales business are operated together so as to constitute one business, tax will apply to the sale of the assets of the business. For example, if a car wash and gasoline station are operated at the same premises and the car wash is available only to persons who buy gasoline or if the price of the car wash is reduced if gasoline is purchased, tax applies to the sale of the car wash.</p>

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	<p><u>3. A person purchases a hardware store with the intent of selling tangible personal property. The person must hold a seller's permit regardless of the number of sales of tangible personal property actually made. For example, if the person makes only two sales, a sale of a hammer and a sale of the business, neither sale is an occasional sale.</u></p> <p><u>4. A person intends to create and sell custom furniture. The person must hold a seller's permit for all his or her sales of furniture. This is true even if, because of the time necessary to create each piece of furniture and the profit resulting from each sale, the person averages one sale of furniture per year.</u></p> <p>(6) TRANSFER OF SHARES IN A CORPORATION. The sale of stock of a corporation is not a sale of tangible personal property and is not subject to sales tax. A stock purchase is not a purchase of tangible personal property and is not subject to sales or use tax notwithstanding the fact that the stock purchase may be treated as an asset acquisition for federal income tax purposes pursuant to Internal Revenue Code Section 338.</p> <p>(b) SALE OR REORGANIZATION OF ALL OR PART OF A BUSINESS.</p> <p>(1) GENERAL. In general, when a person sells a business which is required to hold a seller's permit, tax applies to the gross receipts from the retail sale of tangible personal property held or used by that business in the course of its activities requiring the holding of the seller's permit. The gross receipts from the sale of the business include all consideration received by the transferor, including cash, notes, and any other property as well as any indebtedness assumed by the transferee. It is irrelevant that the indebtedness assumed may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. That is, the transferor is selling a business, and all consideration received is for that business. The measure of tax is the price agreed to by the parties. In the absence of an agreement as to the price of the tangible personal property, the gross receipts from that sale is allocated among the taxable portion and the nontaxable portion by dividing the selling price of the tangible personal property acquired by the purchaser for use rather than resale by the selling price of the entire business sold, and then multiplying that amount by the total gross receipts (i.e., all consideration) received for the business. Book value will be regarded as establishing the price of properties sold. (See Regulation 1610 for special</p>

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	<p>rules applicable to sales of vehicles, vessels, and aircraft.)</p> <p>(2) TRANSFERS OF SUBSTANTIALLY ALL PROPERTY WITHOUT SUBSTANTIAL CHANGE IN OWNERSHIP. Tax does not apply to a transfer of all or substantially all the property held or used by a person in the course of activities for which the person is required to hold a seller's permit or permits or would be required to hold a seller's permit or permits if the activities were conducted in this state, provided that after the transfer the real or ultimate ownership of the property is substantially similar to that which existed before such transfer. “Substantially all the property” means 80 percent or more of all the tangible personal property held or used by the person in the course of activities requiring the holding of a seller's permit, including tangible personal property located outside of this state. If a person engages in two or more separate selling activities, for each of which the person is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state, a transfer of 80 percent or more of the tangible personal property held or used in the combined activities must be made in order to qualify for the exemption described in this paragraph. If a person simultaneously transfers all or substantially all of its assets to more than one entity, the transfer will qualify for the exemption if the ownership remains substantially similar. Stockholders, bondholders, partners, or other persons holding an ownership interest rather than a security interest in the corporation or other entity are regarded as having the real or ultimate ownership of the property of the corporation or other entity.</p> <p>The real or ultimate ownership is “substantially similar” to that which existed before a transfer if 80 percent or more of that ownership of the tangible personal property is unchanged after the transfer. In the following example, the ownership is “substantially similar” to that which existed before the transfer:</p> <table><tr><td></td><td>Interests in</td><td>Interests in</td><td>Interests Common</td></tr><tr><td>Stock-</td><td>Transferor</td><td>Transferee</td><td>Before and After</td></tr><tr><td>holders</td><td>Corporation</td><td>Corporation</td><td>Transfer</td></tr><tr><td>A</td><td>40%</td><td>33 1/3%</td><td>33 1/3%</td></tr><tr><td>B</td><td>40%</td><td>33 1/3%</td><td>33 1/3%</td></tr><tr><td>C</td><td>20%</td><td>33 1/3%</td><td>20%</td></tr><tr><td></td><td>100%</td><td>100%</td><td>86 2/3%</td></tr></table>		Interests in	Interests in	Interests Common	Stock-	Transferor	Transferee	Before and After	holders	Corporation	Corporation	Transfer	A	40%	33 1/3%	33 1/3%	B	40%	33 1/3%	33 1/3%	C	20%	33 1/3%	20%		100%	100%	86 2/3%
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	<p>(3) STATUTORY MERGER. A transfer pursuant to a statutory merger is not a sale but is instead a transfer by operation of law. Thus, tax does not apply to a transfer of property of a constituent corporation to a surviving corporation or new corporation pursuant to a statutory merger under Sections 6010-6022, 1100-1305, or 15678.1-15678.9 of the California Corporations Code or similar laws of this state or other states. The surviving corporation stands in the place of each constituent corporation (including the disappearing corporation(s)). As a result, if property acquired by the surviving corporation in the merger had been purchased and held by the constituent corporation for resale, then the surviving corporation must report and pay use tax on the constituent corporation's purchase price if it makes any use of such resale property, just as the constituent corporation would have owed such tax if it had used the property. Similarly, if the constituent corporation had avoided paying tax measured by the purchase price of mobile transportation equipment by making a timely election to report tax on the fair rental value, the surviving corporation must continue to report tax measured by the fair rental value on its leases of the mobile transportation equipment; if the surviving corporation makes any use of that mobile transportation equipment other than leasing it to another person, the surviving corporation must report tax on the purchase price paid by the constituent corporation.</p> <p>(4) CONTRIBUTION TO COMMENCING CORPORATION, LIMITED LIABILITY COMPANY, PARTNERSHIP, OR JOINT VENTURE. The transfer of tangible personal property to a commencing corporation, commencing limited liability company, commencing partnership, or commencing joint venture in exchange solely for first issue stock of the commencing corporation or an interest in the commencing limited liability company, partnership, or joint venture is not a sale since the interest received by the transferor is not regarded as having measurable value at the time of the transfer. The transferor is the consumer of such property. However, such a transfer is a sale if the transferor receives any consideration, such as cash, notes, or an assumption of indebtedness (whether or not the transferor retains any joint liability with respect to the indebtedness assumed by the transferee), and tax applies to that sale unless it otherwise qualifies for exemption. For purposes of determining the measure of tax from the sale, it is irrelevant that any of the transferor's indebtedness assumed by the transferee may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. The gross receipts from that sale is allocated among the taxable portion and the nontaxable portion by dividing the selling</p>

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	<p>price of the tangible personal property transferred to the purchaser for use rather than for resale by the selling price of all property transferred and then multiplying that amount by the total gross receipts (i.e., all consideration) received by the transferor.</p> <p>When the transferor is a consumer under the previous paragraph, no tax applies with respect to the transfer provided the transferor's use of the property in California would not otherwise be subject to tax. For example, in the case of property purchased by the transferor for resale without payment of the tax, the transferor is the consumer of such property which the transferee will not sell. Since the transferor's use of such resale inventory is subject to tax, the transferor owes tax measured by its purchase price. However, no tax applies with respect to the transfer of such resale inventory provided the transferee will sell such property without any use other than retention, demonstration, and display while holding the property for sale. If the transferee thereafter makes any other use of such property, it must report use tax measured by the transferor's purchase price.</p> <p>(5) DISSOLUTION OF CORPORATION. A distribution of assets, including tangible personal property, by a corporation upon its dissolution to its stockholders in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the corporation other than the stockholders' return of stock certificates for purposes of cancellation. The corporation is the consumer of such property and no tax applies with respect to the transfer provided the corporation's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the stockholders, tax applies measured by that consideration.</p> <p>(6) DISSOLUTION OF LIMITED LIABILITY COMPANY. A distribution of assets, including tangible personal property, by a limited liability company upon its dissolution to its members (i.e., persons holding membership interests and persons holding economic interests) in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the limited liability company other than cancellation of the members' interests. The limited liability company is the consumer of such property and no tax applies with respect to the transfer provided the limited liability company's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the members, tax applies measured by that consideration.</p>

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	<p>(7) DISSOLUTION OF PARTNERSHIP. A partnership is a person for sales and use tax purposes. (Revenue and Taxation Code Section 6005.) However, a partnership is defined for general law purposes as an association of two or more persons to carry on as co-owners a business for profit. (Corporations Code Section 15006.) Dissolution of a partnership is caused by withdrawal of a partner or admission of a new partner, unless otherwise provided in an agreement in writing signed by all the partners, including any such withdrawing partner or any such newly admitted partner before such withdrawal or admission. (Corporations Code Section 15031(7).)</p> <p>Under Corporations Code Section 15026, a partner's interest in the partnership is the partner's share of the profits and surplus, and is personal property. Under Corporations Code Section 15027(1), a conveyance by a partner of that partner's interest in the partnership does not in itself dissolve the partnership, nor, as against the other partners in the absence of agreement, entitle the assignee, during the continuance of the partnership, to interfere in the management or administration of the partnership business or affairs, or to require any information or account of partnership transactions, or to inspect the partnership books; but it merely entitles the assignee to receive in accordance with the partnership contract the profits to which the assigning partner would otherwise be entitled. The assignment of a partnership interest in this technical sense is not a sale of tangible personal property and is not subject to tax.</p> <p>In common usage, however, the term "partnership interest" refers to all of the rights of a partner including (1) the person's rights in specific partnership property, (2) the person's interest (in the technical sense) in the partnership, and (3) the person's right to participate in the management. In a typical commercial transaction when a partner "sells the person's interest in a partnership" to another, it is intended that the person "selling the interest" will withdraw from the partnership and the person "purchasing the interest" will be admitted to the partnership. The legal effect of this transaction is to dissolve the first partnership and to create a new partnership, in the absence of a provision in the agreement providing for continued life of the partnership. The effect for sales and use tax purposes is that there is a dissolution of the partnership, a distribution of the assets on a pro rata basis, and a sale by the withdrawing partner of the person's ownership interest in the tangible personal property distributed to that person. Except as provided in subdivision (c), this sale of tangible personal property will qualify as an occasional sale under Revenue and Taxation Code Section 6006.5 and will be nontaxable under Section 6367, unless</p>

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	<p>the withdrawing partner holds a seller's permit or the sale of tangible personal property is one of a series of sales sufficient in number, scope, and character to require the holding of a seller's permit.</p> <p>A distribution of assets, including tangible personal property, by a partnership upon its dissolution to the partners in accordance with their ownership interests in the partnership is a liquidating dividend and is not a sale when no consideration is received by the partnership other than cancellation of the partners' interests. The partnership is the consumer of such property and no tax applies with respect to the transfer provided the partnership's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the partners, tax applies measured by that consideration.</p> <p>Where a partnership distributes some of its assets in the form of a partial liquidation of the business, the transfer will be regarded as a liquidating dividend, subject to the rules set forth in the previous paragraph, if an entire segment of the business of the partnership is being liquidated. For example, a partnership operates a lumberyard and an automobile repair and parts business. If the partnership ceases operation of the lumberyard and distributes its assets to the partners in accordance with their interest in the partnership and the partnership receives no consideration from the partners such as an assumption of liabilities, the transfer is a liquidating dividend subject to the rules set forth in the previous paragraph. If, however, the partnership ceases operating the repair portion of the automobile repair and parts business and distributes the assets of that portion of the business, it is not liquidating an entire segment of its business and the transfer does not qualify as a nontaxable liquidating dividend.</p> <p>(8) DISSOLUTION OF JOINT VENTURE. For purposes of this paragraph, a joint venture is an undertaking by two or more persons jointly to carry out a single enterprise for profit. The rules applicable to a partnership's liquidating dividends apply to a joint venture's liquidating dividends. The distribution of assets by a joint venture will be regarded as a liquidating dividend, subject to the rules set forth for partnerships, provided at least 80 percent of the purpose of the joint venture has been completed at the time of the distribution. The distribution of the assets of a joint venture prior to 80 percent completion of the purpose of the joint venture cannot qualify as a liquidating dividend and is a sale transaction subject to tax.</p>

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***Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a Seller's Permit (Regulation 1595)***

Action Item	Staff's Proposed Regulatory Language
	<p>(9) SALE FOLLOWING LIQUIDATION. Except as provided in subdivision (c), the transferee's sale of assets acquired in a transfer qualifying as a liquidating dividend, as discussed in this regulation, would be an exempt occasional sale if the property is not sold as part of an activity requiring the holding of a seller's permit and is not one of a series of sales requiring the holding of a seller's permit.</p> <p>(c) VEHICLES, MOBILEHOMES, COMMERCIAL COACHES, VESSELS, AND AIRCRAFT. There is no occasional sale exemption for the sale or use of vehicles required to be registered with the Department of Motor Vehicles, or off-highway vehicles subject to identification under Division 16.5 of the Vehicle Code, mobilehomes and commercial coaches required to be registered with the Department of Housing and Community Development, vessels, or aircraft, as defined by the law and in Regulation 1610 (18 CCR 1610) or in Regulation 1610.2 (18 CCR 1610.2), except when such property is included in a transfer of all or substantially all the property held or used in the course of business activities of the person selling the property and the real or ultimate ownership of the property is substantially similar to that which existed before such transfer. The rules set forth in subdivision (b)(2) of this regulation are applicable in determining under this paragraph whether a transfer is of substantially all the property and whether the ownership is substantially similar.</p> <p>(d) MANUFACTURERS AND WHOLESALERS. A manufacturer, wholesaler, or other person in the business of making sales for resale of tangible personal property of a kind the retail sale of which is taxable whether or not the property is ever sold at retail or is suitable for sale at retail, is liable for tax measured by receipts from any of the person's retail sales of tangible personal property.</p> <p>(e) PRODUCERS OF HAY. A producer of hay is required to hold a seller's permit by reason of the producer's sales of hay, regardless of whether the hay is sold for resale or at retail, and regardless of whether the hay sold at retail constitutes feed for any form of animal life of a kind the products of which ordinarily constitute food for human consumption, unless, operative April 1, 1996, the producer is a grower who produces hay for sale only to beef cattle feedlots or dairies or is a grower who sells exclusively through a farmer-owned cooperative.</p> <p>However, an occasional sale includes a sale of property by a producer of hay, other than hay, provided that the sale is not one of a series of sales sufficient in number, scope, or character to</p>

**AGENDA — July 25, 2000 Business Taxes Committee Meeting**  
***Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a Seller's Permit (Regulation 1595)***

Action Item	Staff's Proposed Regulatory Language
	<p>constitute an activity for which the producer would be required to hold a seller's permit if the producer were not also selling hay.</p> <p>The producer's sale of tangible personal property held or used in the course of an activity of producing the hay (such as farm equipment and machinery) is an occasional sale, provided all of the following conditions apply:</p> <p>(1) The sale is not one of three or more sales of tangible personal property (other than hay) for substantial amounts in any period of 12 months.</p> <p>(2) The sale is not one of a substantial number of sales of tangible personal property (other than hay) for relatively small amounts in any period of 12 months.</p> <p>(3) The tangible personal property was not also held or used in the course of an activity (other than the production of hay) for which a seller's permit is required, or would be required if the activity were conducted in this state.</p>

Issue Paper Number 00 - 022



- ☐ Board Meeting
- ☒ Business Taxes Committee
- ☐ Customer Services and Administrative Efficiency Committee
- ☐ Legislative Committee
- ☐ Property Tax Committee
- ☐ Other

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## **PROPOSED CHANGES TO CLARIFY THE APPLICATION OF TAX TO SALES REQUIRING A SELLER'S PERMIT REGULATION 1595, *OCCASIONAL SALES—SALE OF A BUSINESS—BUSINESS REORGANIZATION***

### **I. Issue**

Should Regulation 1595, *Occasional Sales-Sale of a Business-Business Reorganization*, be revised to recognize the first two sales in a series of sales requiring a seller's permit as occasional sales?

### **II. Staff Recommendation**

Adopt staff's and industry's proposed revisions to Regulation 1595, *Occasional Sales-Sale of a Business-Business Reorganization*, to recognize the first two sales in a series of sales requiring a seller's permit as occasional sales. This proposed regulation revision has no operative date.

### **III. Other Alternative(s) Considered**

Do not adopt proposed revisions to Regulation 1595, *Occasional Sales-Sale of a Business-Business Reorganization*.

## IV. Background

### History of Regulation 1595 – Sales Requiring a Seller’s Permit

Regulation 1595 was first enacted in 1947 (under Ruling No. 81) to interpret and explain the application of tax to the sale of a business and to occasional sales under Revenue and Taxation Code (RTC) section 6006.5. RTC section 6006.5, “*Occasional sale*,” provides that an occasional sale includes a sale of property, not held or used by a seller in an activity requiring a seller’s permit, that is not one of a series of sales sufficient in number, scope, and character to constitute an activity for which he or she is required to hold a seller’s permit or would be required to hold a permit if the activities were conducted in this state. RTC section 6367 exempts from sales and use tax an “occasional sale” under RTC section 6006.5 (except for sales of vehicles, vessels, or aircraft, which are not at issue in the present discussion).

In 1969, language was added to the regulation requiring a person who makes three or more sales for substantial amounts in a period of 12 months to hold a seller’s permit. In 1983, Assembly Bill 1133 overturned the court decision in *Glass-Tite Industries, Inc. v. State Board of Equalization* (1968) 266 Cal.App.2d 691 to define “seller” to include any person engaged in the business of selling tangible personal property “of a kind the gross receipts from the retail sale of which is, or would be, required to be included in the measure of the sales tax if sold at retail, whether or not the tangible personal property is ever sold at retail or is suitable for sale at retail.” This change made it clear that whether a person’s sale qualified as an exempt occasional sale was not dependent on whether that person had ever made a sale at retail, nor whether the property that had been sold by that person was even suitable for sale at retail. In 1984, subdivision (a)(4) of the regulation was added to clarify that tax applied to **all** sales in a series of sales sufficient in number, scope, and character to require the holding of a seller’s permit. This is the rule under review in this paper.

### Current Application of Tax

Subdivision (a)(4)(A) defines the minimum number of sales as follows:

“Generally the minimum number of sales to require the holding of a seller’s permit by a person not otherwise engaged in a selling activity is three within any 12 month period.”

Subdivision (a)(4) of Regulation 1595 states:

“When a person not otherwise engaged in an activity requiring the holding of a seller’s permit makes a series of sales sufficient in number, scope, and character to require the holding of a seller’s permit, the gross receipts from all of such sales are subject to tax.”

Under these provisions, any person qualifying as a “seller”, such as a person who makes a series of three or more substantial sales in any 12 month period, owes tax on all sales in that series, even the first two, unless there is some other basis for exemption or exclusion (such as a sale for resale or a sale in interstate commerce). The first and second sale in a series of sales in a 12-month period requiring the holding of a permit have *not* been considered occasional sales.



**FORMAL ISSUE PAPER**Issue Paper Number 00 - 022Industry's Proposal

Mr. Eric Miethke of the Law Offices of Nielson, Merksamer, Parrinello, Mueller & Naylor, LLP, representing the Motion Picture Association of America (hereafter referred to as industry), proposed revisions to Regulation 1595 that would provide that the first two sales in a series of sales requiring a seller's permit qualify as occasional sales that are exempt from tax.

This issue was an area of disagreement in proposed revisions to Audit Manual Chapter 10, which went before the Business Taxes Committee (BTC) on May 2, 2000. The BTC recognized that industry's proposed change must be addressed through the regulatory process and not through revisions to the Audit Manual. Therefore, Regulation 1595 was put on the BTC's July 25, 2000 agenda.

Industry's proposal was discussed at an interested parties' meeting on May 23, 2000.

Industry feels that it is unreasonable to treat a person whose close-out sale is the third substantial sale in a 12 month period as owing sales tax on the first two sales in that series, when the person would not necessarily have known at the time of those first two sales that they would be part of a series of sales requiring a permit. Industry believes that the current regulation creates inequities. The seller is frequently unable to collect sales tax reimbursement since the seller did not know at the time of the initial sales that more than two sales were going to be made in a 12-month period. If tax is collected on the first sale, the seller is collecting excess tax reimbursement since tax is not currently due and may never be due if more than two sales are not made. Industry also believes that there is no statutory language preventing the first two sales in a series of sales requiring a permit from qualifying as occasional sales. After an analysis of the issues, staff concurs with industry and has addressed these concerns in the revised regulation.

**V. Staff Recommendation****A. Description of the Staff Recommendation**

Adopt staff's and industry's proposed revisions to Regulation 1595, *Occasional Sales-Sale of a Business-Business Reorganization*, to recognize the first two sales in a series of sales requiring a seller's permit as occasional sales. This proposed regulation has no operative date.

A comparison of the current and proposed language of Regulation 1595 is provided in Exhibit 2.

**B. Pros of the Staff Recommendation**

Provides reasonable application of tax to persons who may not be aware at the time of the first and second sale of tangible personal property that they might be part of a series of sales requiring a seller's permit.

**C. Cons of the Staff Recommendation**

- Requires regulatory change.
- Taxpayers that make infrequent sales and are aware of this provision could effectively avoid taxes by how they structure the number and quantity of sales.

**FORMAL ISSUE PAPER**

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**D. Statutory or Regulatory Change**

No statutory change is required. Proposed revisions to Regulation 1595, *Occasional Sales-Sale of a Business-Business Reorganization*, are presented as Exhibit 3.

**E. Administrative Impact**

Staff will be required to notify taxpayers of amendments to the regulation.

**F. Fiscal Impact**

**1. Cost Impact**

Costs related to the amended regulation are absorbable.

**2. Revenue Impact**

See Revenue Estimate (Exhibit 1).

**G. Taxpayer/Customer Impact**

Taxpayers who make infrequent sales may be positively impacted

**H. Critical Time Frames**

Implementation will be upon approval by the Office of Administrative Law (OAL).

The proposed change represents an interpretation of existing statutes, and therefore has no operative date.

**VI. Alternative 1**

**A. Description of the Alternative**

Do not adopt proposed Regulation 1595, *Occasional Sales-Sale of a Business-Business Reorganization*.

**B. Pros of the Alternative**

Current interpretation remains unchanged.

**C. Cons of the Alternative**

Does not eliminate the perceived inequity of imposing tax on sales which, at the time they occur, neither the seller nor the purchaser may know will be taxable.

**D. Statutory or Regulatory Change**

None.

**E. Administrative Impact**

None.

**FORMAL ISSUE PAPER**

Issue Paper Number 00 - 022

**F. Fiscal Impact**

**1. Cost Impact**

None.

**2. Revenue Impact**

None.

**G. Taxpayer/Customer Impact**

Taxpayers who make infrequent or occasional sales will continue to be required to remit sales tax on sales made prior to their registration with the Board.

**H. Critical Time Frames**

None.

Prepared by: Program Planning Division, Sales and Use Tax Department

Current as of: 7/10/2000

**REVENUE ESTIMATE**

STATE OF CALIFORNIA  
BOARD OF EQUALIZATION



**PROPOSED CHANGES TO CLARIFY THE APPLICATION OF TAX  
TO SALES REQUIRING A SELLER'S PERMIT  
REGULATION 1595, *OCCASIONAL SALES – SALE OF A BUSINESS*  
– *BUSINESS REORGANIZATION***

**Staff Recommendation**

Adopt staff's and industry's proposed revisions to Regulation 1595, *Occasional Sales-Sale of a Business-Business Reorganization*, to recognize the first two sales in a series of sales requiring a seller's permit as occasional sales. This proposed regulation revision has no operative date.

**Alternative 1:**

Do not adopt proposed revisions to Regulation 1595, Occasional Sales-Sale of a Business-Business Reorganization.

**Background, Methodology, and Assumptions**

**Staff Recommendation:**

The staff recommendation would provide that only the third and subsequent substantial sales in any 12-month period would be taxable and the first two would not be subject to tax. This proposal would result in a loss of sales and use tax revenue. Unfortunately, the Board has no data on this issue. We do not know how many nonpermitized businesses would make sales that would qualify them for this exemption. However, there are many nonpermitized businesses in California. If a nonpermitized business sells all or nearly all of its assets in a first sale, then sells a few assets in subsequent sales, the initial two sales would not be subject to tax under this proposal. Therefore, this proposal does create the potential for a revenue loss.

**Alternative 1:**

Alternative 1 would have no revenue impact.

## **Revenue Summary**

### **Staff Recommendation:**

There is a potential revenue loss associated with making sales subject to tax beginning with the third substantial, nonexempt sale in a 12-month period.

The effect of this proposal would be retroactive and would create a potential for refunds for 3 years.

### **Alternative 1:**

Alternative 1 has no revenue effect.

## **Preparation**

This revenue estimate was prepared by David E. Hayes, Statistics Section, Agency Planning and Research Division. This revenue estimate was reviewed by Ms. Laurie Frost, Chief, Agency Planning and Research Division and Ms. Charlotte Paliani, Program Planning Manager, Sales and Use Tax Department. For additional information, please contact Mr. Hayes at (916) 445-0840.

Current as of July 10, 2000

**Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a Seller's Permit (Regulation 1595)**

**Comparison of Current and Proposed Language**

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
<p>Action 1 — Consent Adopt Amendments to Proposed Regulation 1595, <i>Occasional Sales – Sale of a Business – Business Reorganization</i></p>	<p>Regulation 1595.</p> <p>Occasional Sales--Sale of a Business— Business Reorganization.</p> <p>(a) ACTIVITIES REQUIRING SELLER'S PERMIT.</p> <p>(1) GENERAL. Tax applies to all retail sales of tangible personal property including capital assets whether sold in one transaction or in a series of sales, held or used by the seller in the course of an activity or activities for which a seller's permit or permits is required or would be required if the activity or activities were conducted in this state. See subdivision (e) below for special rules regarding sales of property by producers of hay.</p> <p>Generally, a person who makes three or more sales for substantial amounts in a period of 12 months is required to hold a seller's permit regardless of whether the sales are at retail or are for resale. Each sale of the person during the 12 month period is included in determining whether that person is required to hold a permit, or would be required to hold a permit if the activities were conducted entirely inside this state. Thus, a sale occurring outside California, whether at retail or for resale, is included, even though it would not be subject to California sales tax. A person who makes a substantial number of sales for relatively small amounts is also required to hold a seller's permit.</p>	<p>Regulation 1595.</p> <p>Occasional Sales--Sale of a Business— Business Reorganization.</p> <p>(a) ACTIVITIES REQUIRING SELLER'S PERMIT.</p> <p>(1) GENERAL. Tax applies to all retail sales of tangible personal property including capital assets whether sold in one transaction or in a series of sales, held or used by the seller in the course of an activity or activities for which a seller's permit or permits is required or would be required if the activity or activities were conducted in this state. See subdivision (e) below for special rules regarding sales of property by producers of hay.</p> <p>Generally, a person who makes three or more sales for substantial amounts in a period of 12 months is required to hold a seller's permit regardless of whether the sales are at retail or are for resale. Each sale of the person during the 12 month period is included in determining whether that person is required to hold a permit, or would be required to hold a permit if the activities were conducted entirely inside this state. Thus, a sale occurring outside California, whether at retail or for resale, is included, even though it would not be subject to California sales tax. A person who makes a substantial number of sales for relatively small amounts is also required to hold a seller's permit.</p>	<p>Regulation is proposed by staff and agreed with by industry. The regulation as proposed by staff now recognizes the first two sales in a series of sales requiring a Seller's Permit as occasional sales.</p>

# Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a Seller's Permit (Regulation 1595)

## Comparison of Current and Proposed Language

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
	<p>Tax does not apply to a sale of property held or used in the course of an activity not requiring the holding of a seller's permit unless the sale is one of a series of sales sufficient in number, scope and character to constitute an activity for which the seller is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state. If tangible personal property is leased under a lease which is a "sale" as defined in Revenue and Taxation Code Section 6006 or a "purchase" as defined in Revenue and Taxation Code Section 6010, tax applies to the lease as provided in Regulation 1660 (18 CCR 1660), and the lessor must hold a seller's permit as provided in Regulation 1699 (18 CCR 1699). The lessor is not making an occasional sale since the lessor is making a "continuing sale" and is thereby holding the leased property in an activity requiring the holding of a seller's permit. As such, the lessor's sale of the leased property at the end of the lease term is likewise not an occasional sale.</p> <p>(2) PROPERTY HELD OR USED IN AN ACTIVITY, OR ACTIVITIES REQUIRING THE HOLDING OF A SELLER'S PERMIT. A seller's permit is required of a person engaged in the business of selling tangible personal property. An activity requiring the holding of that permit includes, but is not limited to, the acquisition and sale of tangible personal property, whether the person's sales are all at retail, all for resale, or include both sales at retail and sales for resale.</p> <p>Acquisition includes the obtaining of the property in any manner whatsoever. For example, raw materials may be purchased or may be obtained by</p>	<p>Tax does not apply to a sale of property held or used in the course of an activity not requiring the holding of a seller's permit unless the sale is one of a series of sales sufficient in number, scope and character to constitute an activity for which the seller is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state. If tangible personal property is leased under a lease which is a "sale" as defined in Revenue and Taxation Code Section 6006 or a "purchase" as defined in Revenue and Taxation Code Section 6010, tax applies to the lease as provided in Regulation 1660 (18 CCR 1660), and the lessor must hold a seller's permit as provided in Regulation 1699 (18 CCR 1699). The lessor is not making an occasional sale since the lessor is making a "continuing sale" and is thereby holding the leased property in an activity requiring the holding of a seller's permit. As such, the lessor's sale of the leased property at the end of the lease term is likewise not an occasional sale.</p> <p>(2) PROPERTY HELD OR USED IN AN ACTIVITY, OR ACTIVITIES REQUIRING THE HOLDING OF A SELLER'S PERMIT. A seller's permit is required of a person engaged in the business of selling tangible personal property. An activity requiring the holding of that permit includes, but is not limited to, the acquisition and sale of tangible personal property, whether the person's sales are all at retail, all for resale, or include both sales at retail and sales for resale.</p> <p>Acquisition includes the obtaining of the property in any manner whatsoever. For example, raw materials may be purchased or may be obtained by</p>	

**Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a  
Seller's Permit (Regulation 1595)  
Comparison of Current and Proposed Language**

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
	<p>extraction from the earth, air or waters of the earth. These may be sold in raw form or processed or manufactured into other raw materials, component parts or finished items which are sold. Each of these activities is an activity which is so related to the sale of tangible personal property, that it is part of the activity requiring the holding of a seller's permit.</p> <p>(3) SEPARATE BUSINESSES. A person engaged in an activity or activities requiring the holding of a seller's permit or permits may also be engaged in entirely separate endeavors which do not require the holding of a seller's permit or permits. Tax applies to the sale of tangible personal property held or used in the course of an activity requiring the holding of a seller's permit. Tax does not apply to the sale of property held or used by the seller in the non-selling endeavors which do not require the holding of a permit unless that sale is itself one of a series of sales requiring the holding of a seller's permit. For example, a person may own a hardware store at one location and a real estate brokerage business at another location, with no relationship between the two activities except that of common ownership. Under these circumstances, a sale of furniture used in the brokerage business would not be a sale of property held or used in an activity requiring the holding of a seller's permit unless it was one of a series of sales of the property of the brokerage business. A sale of tangible personal property held or used in the hardware business would be a sale of property held or used in an activity requiring the holding of a seller's permit.</p>	<p>extraction from the earth, air or waters of the earth. These may be sold in raw form or processed or manufactured into other raw materials, component parts or finished items which are sold. Each of these activities is an activity which is so related to the sale of tangible personal property, that it is part of the activity requiring the holding of a seller's permit.</p> <p>(3) SEPARATE BUSINESSES. A person engaged in an activity or activities requiring the holding of a seller's permit or permits may also be engaged in entirely separate endeavors which do not require the holding of a seller's permit or permits. Tax applies to the sale of tangible personal property held or used in the course of an activity requiring the holding of a seller's permit. Tax does not apply to the sale of property held or used by the seller in the non-selling endeavors which do not require the holding of a permit unless that sale is itself one of a series of sales requiring the holding of a seller's permit. For example, a person may own a hardware store at one location and a real estate brokerage business at another location, with no relationship between the two activities except that of common ownership. Under these circumstances, a sale of furniture used in the brokerage business would not be a sale of property held or used in an activity requiring the holding of a seller's permit unless it was one of a series of sales of the property of the brokerage business. A sale of tangible personal property held or used in the hardware business would be a sale of property held or used in an activity requiring the holding of a seller's permit.</p>	



# Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a Seller's Permit (Regulation 1595)

## Comparison of Current and Proposed Language

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
	<p>(4) SERIES OF SALES REQUIRING THE HOLDING OF A SELLER'S PERMIT. When a person not otherwise engaged in an activity requiring the holding of a seller's permit makes a series of sales sufficient in number, scope and character to require the holding of a seller's permit, the gross receipts from all of such sales are subject to tax.</p> <p>(A) Number.</p> <p>1. Generally the minimum number of sales to require the holding of a seller's permit by a person not otherwise engaged in a selling activity is three within any 12 month period.</p> <p>2. When calculating the minimum number of sales which requires a person to hold a seller's permit, the following types of sales are excluded:</p> <p>a. Sales made by an auctioneer on behalf of the person. In such transactions, the auctioneer is the retailer liable for tax.</p> <p>b. Sales through claiming races of horses owned by the person. In such transactions, the racing association is the retailer liable for tax.</p> <p>c. Sales of vehicles, mobilehomes, commercial coaches, vessels, or aircraft which are exempted from sales tax by Revenue and Taxation Code Sections 6282 and 6283.</p> <p>d. A trade-in made by the person which is incidental to a nonselling activity of the person.</p> <p>(B) Scope. The extent of the sales measured by</p>	<p>(4) SERIES OF SALES REQUIRING THE HOLDING OF A SELLER'S PERMIT. <del>When a</del><u>A</u> person not otherwise engaged in an activity requiring the holding of a seller's permit <del>may make</del><u>may make</u> <del>makes</del> a series of sales sufficient in number, scope and character to require the holding of a seller's permit, <del>the gross receipts from all of such sales are subject to tax.</del> <u>The sale in that series of sales, and subsequent sales, during any 12 month period which resulted in the requirement to hold a permit are subject to tax, unless otherwise exempt.</u></p> <p>(A) Number.</p> <p>1. Generally the minimum number of sales to require the holding of a seller's permit by a person not otherwise engaged in a selling activity is three within any 12 month period.</p> <p>2. When calculating the minimum number of sales which requires a person to hold a seller's permit, the following types of sales are excluded:</p> <p>a. Sales made by an auctioneer on behalf of the person. In such transactions, the auctioneer is the retailer liable for tax.</p> <p>b. Sales through claiming races of horses owned by the person. In such transactions, the racing association is the retailer liable for tax.</p> <p>c. Sales of vehicles, mobilehomes, commercial coaches, vessels, or aircraft which are exempted from sales tax by Revenue and Taxation Code Sections 6282 and 6283.</p> <p>d. A trade-in made by the person which is incidental to a nonselling activity of the person.</p> <p>(B) Scope. The extent of the sales measured by</p>	

**Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a  
Seller's Permit (Regulation 1595)  
Comparison of Current and Proposed Language**

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
	<p>their frequency or dollar volume.</p> <p>(C) Character. This relates to the similarity in type and value giving effect to the taxpayer's operations. For example, a processor of food products for human consumption is not required to hold a seller's permit for the processing and sale of food products. Sales of used lug boxes, obsolete or used machinery, food handling and similar items are of a character that three or more sales of sufficient scope will require the processor to hold a seller's permit for this selling activity.</p> <p>(5) EXAMPLES APPLYING THE ABOVE PRINCIPLES.</p> <p>(A) Service enterprises which make some incidental sales.</p> <p>1. Operators of service enterprises such as hospitals, hotels, theaters, schools, laundromats, car washes, transportation companies, and trucking companies may make some sales incidental to their primary service business. A hospital may operate a pharmacy and cafeteria as an adjunct to the hospital. A hotel may operate a restaurant and a bar. A theater may sell popcorn to patrons. A school may operate a cafeteria and bookstore. A laundromat may sell soap to its customers.</p> <p>If any of these businesses were sold, tax would apply only to the gross receipts from the tangible personal property held or used in the selling activity.</p> <p>2. If, in any 12 month period, the operator of</p>	<p>their frequency or dollar volume.</p> <p>(C) Character. This relates to the similarity in type and value giving effect to the taxpayer's operations. For example, a processor of food products for human consumption is not required to hold a seller's permit for the processing and sale of food products. Sales of used lug boxes, obsolete or used machinery, food handling and similar items are of a character that three or more sales of sufficient scope will require the processor to hold a seller's permit for this selling activity.</p> <p>(5) EXAMPLES APPLYING THE ABOVE PRINCIPLES.</p> <p>(A) Service enterprises which make some incidental sales.</p> <p>1. Operators of service enterprises such as hospitals, hotels, theaters, schools, laundromats, car washes, transportation companies, and trucking companies may make some sales incidental to their primary service business. A hospital may operate a pharmacy and cafeteria as an adjunct to the hospital. A hotel may operate a restaurant and a bar. A theater may sell popcorn to patrons. A school may operate a cafeteria and bookstore. A laundromat may sell soap to its customers.</p> <p>If any of these businesses were sold, tax would apply only to the gross receipts from the tangible personal property held or used in the selling activity.</p> <p>2. If, in any 12 month period, the operator of</p>	

# Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a Seller's Permit (Regulation 1595)

## Comparison of Current and Proposed Language

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
	<p>the service enterprise makes more than two sales in substantial amounts of tangible personal property used in the service enterprise, none of the sales qualify as an occasional sale. The gross receipts from those sales are subject to tax, unless otherwise exempt. For example, if one sale is a sale in interstate commerce, the gross receipts from that sale would be exempt; however, the gross receipts from the other sales would be taxable. If one of the sales is a sale of the business, sales tax applies to the gross receipts from the retail sale of the tangible personal property located in California and use tax applies to the sales price of property purchased for use in California and used in this state.</p>	<p>the service enterprise makes more than two sales in substantial amounts of tangible personal property used in the service enterprise, <del>none of the sales qualify as an occasional sale</del><u>the first two sales are exempt occasional sales, but the operator is required to hold a permit for the third and subsequent sales during any 12 month period. The gross receipts from the third and subsequent those sales during any such 12 month period</u> are subject to tax, unless otherwise exempt. <del>For example, if one sale is a sale in interstate commerce, the gross receipts from that sale would be exempt; however, the gross receipts from the other sales would be taxable. If one of the sales is a sale of the business, sales tax applies to the gross receipts from the retail sale of the tangible personal property located in California and use tax applies to the sales price of property purchased for use in California and used in this state. For example, the only sales that a service enterprise made were the following sales (each of which was "substantial" for purposes of this regulation) of tangible personal property used in the service enterprise:</del></p> <div style="margin-left: 40px;"> <p>a. <u>February 23, 1996</u> Occasional sale</p> <p>b. <u>August 16, 1996</u> Occasional sale</p> <p>c. <u>January 8, 1997</u> Not occasional sale</p> <p>d. <u>February 8, 1997</u> Not occasional sale</p> <p>e. <u>January 27, 1998</u> Occasional sale</p> <p>f. <u>February 3, 1998</u> Not occasional sale</p> </div>	

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Seller's Permit (Regulation 1595)  
Comparison of Current and Proposed Language**

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		<p>g. <u>August 11, 1999</u> <u>Occasional sale</u></p> <p>h. <u>December 12, 1999</u> <u>Occasional sale</u></p> <p>i. <u>September 8, 2000</u> <u>Occasional sale</u></p> <p>j. <u>December 9, 2000</u> <u>Not occasional sale</u></p> <p><u>Sales a. and b. are occasional sales since since they were the first two sales made by the service enterprise.</u></p> <p><u>Sales c. and d. are not occasional sales since they were the third and fourth sales in the series of sales commencing on February 23, 1996, which was less than 12 months prior to these sales.</u></p> <p><u>Sale e. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on February 8, 1997. The January 8, 1997 sale is not relevant since it occurred more than 12 months prior to sale e.</u></p> <p><u>Sale f. is not an occasional sale since it was the third sale in the series of sales commencing on February 8, 1997, which was less than 12 months prior to this sale.</u></p> <p><u>Sale g. is an occasional sale since the service enterprise made no other sales in the prior 12 months.</u></p> <p><u>Sale h. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on August 11, 1999.</u></p>	

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	<p>(B) Other businesses.</p> <p>1. Tax applies to the sales of assets of a business which is not essentially a service enterprise. Examples of this are sales of grocery stores and liquor stores making both exempt sales of food products for human consumption and taxable sales of other tangible personal property, service stations which sell gasoline, oil and similar items and which also perform automotive repairs and lubrication services, and computer stores which also provide training in the use of computers and repairs for computer products.</p> <p>2. Where a service enterprise and a sales business are operated together so as to constitute one business, tax will apply to the sale of the assets of the business. For example, if a car wash and gasoline station are operated at the same premises and the car wash is available only to persons who buy gasoline or if the price of the car wash is reduced if gasoline is purchased, tax applies to the sale of the car wash.</p>	<p><u>Sale i. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on December 12, 1999.</u></p> <p><u>Sale j. is not an occasional sale since it was the third sale in the series of sales commencing within the prior 12 months, on December 12, 1999.</u></p> <p>(B) Other businesses.</p> <p>1. Tax applies to the sales of assets of a business which is not essentially a service enterprise. Examples of this are sales of grocery stores and liquor stores making both exempt sales of food products for human consumption and taxable sales of other tangible personal property, service stations which sell gasoline, oil and similar items and which also perform automotive repairs and lubrication services, and computer stores which also provide training in the use of computers and repairs for computer products.</p> <p>2. Where a service enterprise and a sales business are operated together so as to constitute one business, tax will apply to the sale of the assets of the business. For example, if a car wash and gasoline station are operated at the same premises and the car wash is available only to persons who buy gasoline or if the price of the car wash is reduced if gasoline is purchased, tax applies to the sale of the car wash.</p> <p><u>3. A person purchases a hardware store with the intent of selling tangible personal property.</u></p>	

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	<p>(6) TRANSFER OF SHARES IN A CORPORATION. The sale of stock of a corporation is not a sale of tangible personal property and is not subject to sales tax. A stock purchase is not a purchase of tangible personal property and is not subject to sales or use tax notwithstanding the fact that the stock purchase may be treated as an asset acquisition for federal income tax purposes pursuant to Internal Revenue Code Section 338.</p> <p>(b) SALE OR REORGANIZATION OF ALL OR PART OF A BUSINESS.</p> <p>(1) GENERAL. In general, when a person sells a business which is required to hold a seller's permit, tax applies to the gross receipts from the retail sale of tangible personal property held or used by that business in the course of its activities requiring the holding of the seller's permit. The gross receipts from the sale of the business include</p>	<p><u>The person must hold a seller's permit regardless of the number of sales of tangible personal property actually made. For example, if the person makes only two sales, a sale of a hammer and a sale of the business, neither sale is an occasional sale.</u></p> <p><u>4. A person intends to create and sell custom furniture. The person must hold a seller's permit for all his or her sales of furniture. This is true even if, because of the time necessary to create each piece of furniture and the profit resulting from each sale, the person averages one sale of furniture per year.</u></p> <p>(6) TRANSFER OF SHARES IN A CORPORATION. The sale of stock of a corporation is not a sale of tangible personal property and is not subject to sales tax. A stock purchase is not a purchase of tangible personal property and is not subject to sales or use tax notwithstanding the fact that the stock purchase may be treated as an asset acquisition for federal income tax purposes pursuant to Internal Revenue Code Section 338.</p> <p>(b) SALE OR REORGANIZATION OF ALL OR PART OF A BUSINESS.</p> <p>(1) GENERAL. In general, when a person sells a business which is required to hold a seller's permit, tax applies to the gross receipts from the retail sale of tangible personal property held or used by that business in the course of its activities requiring the holding of the seller's permit. The gross receipts from the sale of the business include</p>	

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	<p>all consideration received by the transferor, including cash, notes, and any other property as well as any indebtedness assumed by the transferee. It is irrelevant that the indebtedness assumed may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. That is, the transferor is selling a business, and all consideration received is for that business. The measure of tax is the price agreed to by the parties. In the absence of an agreement as to the price of the tangible personal property, the gross receipts from that sale is allocated among the taxable portion and the nontaxable portion by dividing the selling price of the tangible personal property acquired by the purchaser for use rather than resale by the selling price of the entire business sold, and then multiplying that amount by the total gross receipts (i.e., all consideration) received for the business. Book value will be regarded as establishing the price of properties sold. (See Regulation 1610 for special rules applicable to sales of vehicles, vessels, and aircraft.)</p> <p>(2) TRANSFERS OF SUBSTANTIALLY ALL PROPERTY WITHOUT SUBSTANTIAL CHANGE IN OWNERSHIP. Tax does not apply to a transfer of all or substantially all the property held or used by a person in the course of activities for which the person is required to hold a seller's permit or permits or would be required to hold a seller's permit or permits if the activities were conducted in this state, provided that after the transfer the real or ultimate ownership of the property is substantially similar to that which</p>	<p>all consideration received by the transferor, including cash, notes, and any other property as well as any indebtedness assumed by the transferee. It is irrelevant that the indebtedness assumed may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. That is, the transferor is selling a business, and all consideration received is for that business. The measure of tax is the price agreed to by the parties. In the absence of an agreement as to the price of the tangible personal property, the gross receipts from that sale is allocated among the taxable portion and the nontaxable portion by dividing the selling price of the tangible personal property acquired by the purchaser for use rather than resale by the selling price of the entire business sold, and then multiplying that amount by the total gross receipts (i.e., all consideration) received for the business. Book value will be regarded as establishing the price of properties sold. (See Regulation 1610 for special rules applicable to sales of vehicles, vessels, and aircraft.)</p> <p>(2) TRANSFERS OF SUBSTANTIALLY ALL PROPERTY WITHOUT SUBSTANTIAL CHANGE IN OWNERSHIP. Tax does not apply to a transfer of all or substantially all the property held or used by a person in the course of activities for which the person is required to hold a seller's permit or permits or would be required to hold a seller's permit or permits if the activities were conducted in this state, provided that after the transfer the real or ultimate ownership of the property is substantially similar to that which</p>	

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	<p>existed before such transfer. "Substantially all the property" means 80 percent or more of all the tangible personal property held or used by the person in the course of activities requiring the holding of a seller's permit, including tangible personal property located outside of this state. If a person engages in two or more separate selling activities, for each of which the person is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state, a transfer of 80 percent or more of the tangible personal property held or used in the combined activities must be made in order to qualify for the exemption described in this paragraph. If a person simultaneously transfers all or substantially all of its assets to more than one entity, the transfer will qualify for the exemption if the ownership remains substantially similar. Stockholders, bondholders, partners, or other persons holding an ownership interest rather than a security interest in the corporation or other entity are regarded as having the real or ultimate ownership of the property of the corporation or other entity.</p> <p>The real or ultimate ownership is "substantially similar" to that which existed before a transfer if 80 percent or more of that ownership of the tangible personal property is unchanged after the transfer. In the following example, the ownership is "substantially similar" to that which existed before the transfer:</p>	<p>existed before such transfer. "Substantially all the property" means 80 percent or more of all the tangible personal property held or used by the person in the course of activities requiring the holding of a seller's permit, including tangible personal property located outside of this state. If a person engages in two or more separate selling activities, for each of which the person is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state, a transfer of 80 percent or more of the tangible personal property held or used in the combined activities must be made in order to qualify for the exemption described in this paragraph. If a person simultaneously transfers all or substantially all of its assets to more than one entity, the transfer will qualify for the exemption if the ownership remains substantially similar. Stockholders, bondholders, partners, or other persons holding an ownership interest rather than a security interest in the corporation or other entity are regarded as having the real or ultimate ownership of the property of the corporation or other entity.</p> <p>The real or ultimate ownership is "substantially similar" to that which existed before a transfer if 80 percent or more of that ownership of the tangible personal property is unchanged after the transfer. In the following example, the ownership is "substantially similar" to that which existed before the transfer:</p>	



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	Stock- Holders	Interests in Transferor Corporation	Interests in Transferee Corporation	Interests Common Before and After Transfer	Stock- Holders	Interests in Transferor Corporation	Interests in Transferee Corporation	Interests Common Before and After Transfer	
	A	40%	33 1/3%	33 1/3%	A	40%	33 1/3%	33 1/3%	
	B	40%	33 1/3%	33 1/3%	B	40%	33 1/3%	33 1/3%	
	C	20%	33 1/3%	20%	C	20%	33 1/3%	20%	
		100%	100%	100%		100%	100%	100%	
	(3) STATUTORY MERGER. A transfer pursuant to a statutory merger is not a sale but is instead a transfer by operation of law. Thus, tax does not apply to a transfer of property of a constituent corporation to a surviving corporation or new corporation pursuant to a statutory merger under Sections 6010-6022, 1100-1305, or 15678.1-15678.9 of the California Corporations Code or similar laws of this state or other states. The surviving corporation stands in the place of each constituent corporation (including the disappearing corporation(s)). As a result, if property acquired by the surviving corporation in the merger had been purchased and held by the constituent corporation for resale, then the surviving corporation must report and pay use tax on the constituent corporation's purchase price if it makes any use of such resale property, just as the constituent corporation would have owed such tax if it had used the property. Similarly, if the constituent corporation had avoided paying tax measured by the purchase price of mobile transportation equipment by making a timely election to report tax on the fair rental value, the surviving corporation must continue to report tax measured by the fair rental value on its leases of the mobile				(3) STATUTORY MERGER. A transfer pursuant to a statutory merger is not a sale but is instead a transfer by operation of law. Thus, tax does not apply to a transfer of property of a constituent corporation to a surviving corporation or new corporation pursuant to a statutory merger under Sections 6010-6022, 1100-1305, or 15678.1-15678.9 of the California Corporations Code or similar laws of this state or other states. The surviving corporation stands in the place of each constituent corporation (including the disappearing corporation(s)). As a result, if property acquired by the surviving corporation in the merger had been purchased and held by the constituent corporation for resale, then the surviving corporation must report and pay use tax on the constituent corporation's purchase price if it makes any use of such resale property, just as the constituent corporation would have owed such tax if it had used the property. Similarly, if the constituent corporation had avoided paying tax measured by the purchase price of mobile transportation equipment by making a timely election to report tax on the fair rental value, the surviving corporation must continue to report tax measured by the fair rental value on its leases of the mobile				

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	<p>transportation equipment; if the surviving corporation makes any use of that mobile transportation equipment other than leasing it to another person, the surviving corporation must report tax on the purchase price paid by the constituent corporation.</p> <p>(4) CONTRIBUTION TO COMMENCING CORPORATION, LIMITED LIABILITY COMPANY, PARTNERSHIP, OR JOINT VENTURE. The transfer of tangible personal property to a commencing corporation, commencing limited liability company, commencing partnership, or commencing joint venture in exchange solely for first issue stock of the commencing corporation or an interest in the commencing limited liability company, partnership, or joint venture is not a sale since the interest received by the transferor is not regarded as having measurable value at the time of the transfer. The transferor is the consumer of such property. However, such a transfer is a sale if the transferor receives any consideration, such as cash, notes, or an assumption of indebtedness (whether or not the transferor retains any joint liability with respect to the indebtedness assumed by the transferee), and tax applies to that sale unless it otherwise qualifies for exemption. For purposes of determining the measure of tax from the sale, it is irrelevant that any of the transferor's indebtedness assumed by the transferee may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. The gross receipts from that sale is allocated among the taxable portion and the</p>	<p>transportation equipment; if the surviving corporation makes any use of that mobile transportation equipment other than leasing it to another person, the surviving corporation must report tax on the purchase price paid by the constituent corporation.</p> <p>(4) CONTRIBUTION TO COMMENCING CORPORATION, LIMITED LIABILITY COMPANY, PARTNERSHIP, OR JOINT VENTURE. The transfer of tangible personal property to a commencing corporation, commencing limited liability company, commencing partnership, or commencing joint venture in exchange solely for first issue stock of the commencing corporation or an interest in the commencing limited liability company, partnership, or joint venture is not a sale since the interest received by the transferor is not regarded as having measurable value at the time of the transfer. The transferor is the consumer of such property. However, such a transfer is a sale if the transferor receives any consideration, such as cash, notes, or an assumption of indebtedness (whether or not the transferor retains any joint liability with respect to the indebtedness assumed by the transferee), and tax applies to that sale unless it otherwise qualifies for exemption. For purposes of determining the measure of tax from the sale, it is irrelevant that any of the transferor's indebtedness assumed by the transferee may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. The gross receipts from that sale is allocated among the taxable portion and the</p>	

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	<p>nontaxable portion by dividing the selling price of the tangible personal property transferred to the purchaser for use rather than for resale by the selling price of all property transferred and then multiplying that amount by the total gross receipts (i.e., all consideration) received by the transferor.</p> <p>When the transferor is a consumer under the previous paragraph, no tax applies with respect to the transfer provided the transferor's use of the property in California would not otherwise be subject to tax. For example, in the case of property purchased by the transferor for resale without payment of the tax, the transferor is the consumer of such property which the transferee will not sell. Since the transferor's use of such resale inventory is subject to tax, the transferor owes tax measured by its purchase price. However, no tax applies with respect to the transfer of such resale inventory provided the transferee will sell such property without any use other than retention, demonstration, and display while holding the property for sale. If the transferee thereafter makes any other use of such property, it must report use tax measured by the transferor's purchase price.</p> <p>(5) DISSOLUTION OF CORPORATION. A distribution of assets, including tangible personal property, by a corporation upon its dissolution to its stockholders in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the corporation other than the stockholders' return of stock certificates for purposes of cancellation. The corporation is the consumer of such property and no tax applies with respect to the transfer provided</p>	<p>nontaxable portion by dividing the selling price of the tangible personal property transferred to the purchaser for use rather than for resale by the selling price of all property transferred and then multiplying that amount by the total gross receipts (i.e., all consideration) received by the transferor.</p> <p>When the transferor is a consumer under the previous paragraph, no tax applies with respect to the transfer provided the transferor's use of the property in California would not otherwise be subject to tax. For example, in the case of property purchased by the transferor for resale without payment of the tax, the transferor is the consumer of such property which the transferee will not sell. Since the transferor's use of such resale inventory is subject to tax, the transferor owes tax measured by its purchase price. However, no tax applies with respect to the transfer of such resale inventory provided the transferee will sell such property without any use other than retention, demonstration, and display while holding the property for sale. If the transferee thereafter makes any other use of such property, it must report use tax measured by the transferor's purchase price.</p> <p>(5) DISSOLUTION OF CORPORATION. A distribution of assets, including tangible personal property, by a corporation upon its dissolution to its stockholders in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the corporation other than the stockholders' return of stock certificates for purposes of cancellation. The corporation is the consumer of such property and no tax applies with respect to the transfer provided</p>	

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	<p>the corporation's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the stockholders, tax applies measured by that consideration.</p> <p>(6) DISSOLUTION OF LIMITED LIABILITY COMPANY. A distribution of assets, including tangible personal property, by a limited liability company upon its dissolution to its members (i.e., persons holding membership interests and persons holding economic interests) in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the limited liability company other than cancellation of the members' interests. The limited liability company is the consumer of such property and no tax applies with respect to the transfer provided the limited liability company's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the members, tax applies measured by that consideration.</p> <p>(7) DISSOLUTION OF PARTNERSHIP. A partnership is a person for sales and use tax purposes. (Revenue and Taxation Code Section 6005.) However, a partnership is defined for general law purposes as an association of two or more persons to carry on as co-owners a business for profit. (Corporations Code Section 15006.) Dissolution of a partnership is caused by withdrawal of a partner or admission of a new partner, unless otherwise provided in an agreement</p>	<p>the corporation's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the stockholders, tax applies measured by that consideration.</p> <p>(6) DISSOLUTION OF LIMITED LIABILITY COMPANY. A distribution of assets, including tangible personal property, by a limited liability company upon its dissolution to its members (i.e., persons holding membership interests and persons holding economic interests) in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the limited liability company other than cancellation of the members' interests. The limited liability company is the consumer of such property and no tax applies with respect to the transfer provided the limited liability company's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the members, tax applies measured by that consideration.</p> <p>(7) DISSOLUTION OF PARTNERSHIP. A partnership is a person for sales and use tax purposes. (Revenue and Taxation Code Section 6005.) However, a partnership is defined for general law purposes as an association of two or more persons to carry on as co-owners a business for profit. (Corporations Code Section 15006.) Dissolution of a partnership is caused by withdrawal of a partner or admission of a new partner, unless otherwise provided in an agreement</p>	

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	<p>in writing signed by all the partners, including any such withdrawing partner or any such newly admitted partner before such withdrawal or admission. (Corporations Code Section 15031(7).)</p> <p>Under Corporations Code Section 15026, a partner's interest in the partnership is the partner's share of the profits and surplus, and is personal property. Under Corporations Code Section 15027(1), a conveyance by a partner of that partner's interest in the partnership does not in itself dissolve the partnership, nor, as against the other partners in the absence of agreement, entitle the assignee, during the continuance of the partnership, to interfere in the management or administration of the partnership business or affairs, or to require any information or account of partnership transactions, or to inspect the partnership books; but it merely entitles the assignee to receive in accordance with the partnership contract the profits to which the assigning partner would otherwise be entitled. The assignment of a partnership interest in this technical sense is not a sale of tangible personal property and is not subject to tax.</p> <p>In common usage, however, the term "partnership interest" refers to all of the rights of a partner including (1) the person's rights in specific partnership property, (2) the person's interest (in the technical sense) in the partnership, and (3) the person's right to participate in the management. In a typical commercial transaction when a partner "sells the person's interest in a partnership" to another, it is intended that the person "selling the interest" will withdraw from the partnership and</p>	<p>in writing signed by all the partners, including any such withdrawing partner or any such newly admitted partner before such withdrawal or admission. (Corporations Code Section 15031(7).)</p> <p>Under Corporations Code Section 15026, a partner's interest in the partnership is the partner's share of the profits and surplus, and is personal property. Under Corporations Code Section 15027(1), a conveyance by a partner of that partner's interest in the partnership does not in itself dissolve the partnership, nor, as against the other partners in the absence of agreement, entitle the assignee, during the continuance of the partnership, to interfere in the management or administration of the partnership business or affairs, or to require any information or account of partnership transactions, or to inspect the partnership books; but it merely entitles the assignee to receive in accordance with the partnership contract the profits to which the assigning partner would otherwise be entitled. The assignment of a partnership interest in this technical sense is not a sale of tangible personal property and is not subject to tax.</p> <p>In common usage, however, the term "partnership interest" refers to all of the rights of a partner including (1) the person's rights in specific partnership property, (2) the person's interest (in the technical sense) in the partnership, and (3) the person's right to participate in the management. In a typical commercial transaction when a partner "sells the person's interest in a partnership" to another, it is intended that the person "selling the interest" will withdraw from the partnership and</p>	

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	<p>the person "purchasing the interest" will be admitted to the partnership. The legal effect of this transaction is to dissolve the first partnership and to create a new partnership, in the absence of a provision in the agreement providing for continued life of the partnership. The effect for sales and use tax purposes is that there is a dissolution of the partnership, a distribution of the assets on a pro rata basis, and a sale by the withdrawing partner of the person's ownership interest in the tangible personal property distributed to that person. Except as provided in subdivision (c), this sale of tangible personal property will qualify as an occasional sale under Revenue and Taxation Code Section 6006.5 and will be nontaxable under Section 6367, unless the withdrawing partner holds a seller's permit or the sale of tangible personal property is one of a series of sales sufficient in number, scope, and character to require the holding of a seller's permit.</p> <p>A distribution of assets, including tangible personal property, by a partnership upon its dissolution to the partners in accordance with their ownership interests in the partnership is a liquidating dividend and is not a sale when no consideration is received by the partnership other than cancellation of the partners' interests. The partnership is the consumer of such property and no tax applies with respect to the transfer provided the partnership's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the partners, tax applies measured by that consideration.</p>	<p>the person "purchasing the interest" will be admitted to the partnership. The legal effect of this transaction is to dissolve the first partnership and to create a new partnership, in the absence of a provision in the agreement providing for continued life of the partnership. The effect for sales and use tax purposes is that there is a dissolution of the partnership, a distribution of the assets on a pro rata basis, and a sale by the withdrawing partner of the person's ownership interest in the tangible personal property distributed to that person. Except as provided in subdivision (c), this sale of tangible personal property will qualify as an occasional sale under Revenue and Taxation Code Section 6006.5 and will be nontaxable under Section 6367, unless the withdrawing partner holds a seller's permit or the sale of tangible personal property is one of a series of sales sufficient in number, scope, and character to require the holding of a seller's permit.</p> <p>A distribution of assets, including tangible personal property, by a partnership upon its dissolution to the partners in accordance with their ownership interests in the partnership is a liquidating dividend and is not a sale when no consideration is received by the partnership other than cancellation of the partners' interests. The partnership is the consumer of such property and no tax applies with respect to the transfer provided the partnership's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the partners, tax applies measured by that consideration.</p>	

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	<p>Where a partnership distributes some of its assets in the form of a partial liquidation of the business, the transfer will be regarded as a liquidating dividend, subject to the rules set forth in the previous paragraph, if an entire segment of the business of the partnership is being liquidated. For example, a partnership operates a lumberyard and an automobile repair and parts business. If the partnership ceases operation of the lumberyard and distributes its assets to the partners in accordance with their interest in the partnership and the partnership receives no consideration from the partners such as an assumption of liabilities, the transfer is a liquidating dividend subject to the rules set forth in the previous paragraph. If, however, the partnership ceases operating the repair portion of the automobile repair and parts business and distributes the assets of that portion of the business, it is not liquidating an entire segment of its business and the transfer does not qualify as a nontaxable liquidating dividend.</p> <p>(8) DISSOLUTION OF JOINT VENTURE. For purposes of this paragraph, a joint venture is an undertaking by two or more persons jointly to carry out a single enterprise for profit. The rules applicable to a partnership's liquidating dividends apply to a joint venture's liquidating dividends. The distribution of assets by a joint venture will be regarded as a liquidating dividend, subject to the rules set forth for partnerships, provided at least 80 percent of the purpose of the joint venture has been completed at the time of the distribution. The distribution of the assets of a joint venture prior to 80 percent completion of the purpose of the joint venture cannot qualify as a liquidating dividend</p>	<p>Where a partnership distributes some of its assets in the form of a partial liquidation of the business, the transfer will be regarded as a liquidating dividend, subject to the rules set forth in the previous paragraph, if an entire segment of the business of the partnership is being liquidated. For example, a partnership operates a lumberyard and an automobile repair and parts business. If the partnership ceases operation of the lumberyard and distributes its assets to the partners in accordance with their interest in the partnership and the partnership receives no consideration from the partners such as an assumption of liabilities, the transfer is a liquidating dividend subject to the rules set forth in the previous paragraph. If, however, the partnership ceases operating the repair portion of the automobile repair and parts business and distributes the assets of that portion of the business, it is not liquidating an entire segment of its business and the transfer does not qualify as a nontaxable liquidating dividend.</p> <p>(8) DISSOLUTION OF JOINT VENTURE. For purposes of this paragraph, a joint venture is an undertaking by two or more persons jointly to carry out a single enterprise for profit. The rules applicable to a partnership's liquidating dividends apply to a joint venture's liquidating dividends. The distribution of assets by a joint venture will be regarded as a liquidating dividend, subject to the rules set forth for partnerships, provided at least 80 percent of the purpose of the joint venture has been completed at the time of the distribution. The distribution of the assets of a joint venture prior to 80 percent completion of the purpose of the joint venture cannot qualify as a liquidating dividend</p>	

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	<p>and is a sale transaction subject to tax.</p> <p>(9) SALE FOLLOWING LIQUIDATION. Except as provided in subdivision (c), the transferee's sale of assets acquired in a transfer qualifying as a liquidating dividend, as discussed in this regulation, would be an exempt occasional sale if the property is not sold as part of an activity requiring the holding of a seller's permit and is not one of a series of sales requiring the holding of a seller's permit.</p> <p>(c) VEHICLES, MOBILEHOMES, COMMERCIAL COACHES, VESSELS, AND AIRCRAFT. There is no occasional sale exemption for the sale or use of vehicles required to be registered with the Department of Motor Vehicles, or off-highway vehicles subject to identification under Division 16.5 of the Vehicle Code, mobilehomes and commercial coaches required to be registered with the Department of Housing and Community Development, vessels, or aircraft, as defined by the law and in Regulation 1610 (18 CCR 1610) or in Regulation 1610.2 (18 CCR 1610.2), except when such property is included in a transfer of all or substantially all the property held or used in the course of business activities of the person selling the property and the real or ultimate ownership of the property is substantially similar to that which existed before such transfer. The rules set forth in subdivision (b)(2) of this regulation are applicable in determining under this paragraph whether a transfer is of substantially all the property and whether the ownership is substantially similar.</p>	<p>and is a sale transaction subject to tax.</p> <p>(9) SALE FOLLOWING LIQUIDATION. Except as provided in subdivision (c), the transferee's sale of assets acquired in a transfer qualifying as a liquidating dividend, as discussed in this regulation, would be an exempt occasional sale if the property is not sold as part of an activity requiring the holding of a seller's permit and is not one of a series of sales requiring the holding of a seller's permit.</p> <p>(c) VEHICLES, MOBILEHOMES, COMMERCIAL COACHES, VESSELS, AND AIRCRAFT. There is no occasional sale exemption for the sale or use of vehicles required to be registered with the Department of Motor Vehicles, or off-highway vehicles subject to identification under Division 16.5 of the Vehicle Code, mobilehomes and commercial coaches required to be registered with the Department of Housing and Community Development, vessels, or aircraft, as defined by the law and in Regulation 1610 (18 CCR 1610) or in Regulation 1610.2 (18 CCR 1610.2), except when such property is included in a transfer of all or substantially all the property held or used in the course of business activities of the person selling the property and the real or ultimate ownership of the property is substantially similar to that which existed before such transfer. The rules set forth in subdivision (b)(2) of this regulation are applicable in determining under this paragraph whether a transfer is of substantially all the property and whether the ownership is substantially similar.</p>	



**Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a  
Seller's Permit (Regulation 1595)  
Comparison of Current and Proposed Language**

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
	<p>(d) MANUFACTURERS AND WHOLESALERS. A manufacturer, wholesaler, or other person in the business of making sales for resale of tangible personal property of a kind the retail sale of which is taxable whether or not the property is ever sold at retail or is suitable for sale at retail, is liable for tax measured by receipts from any of the person's retail sales of tangible personal property.</p> <p>(e) PRODUCERS OF HAY. A producer of hay is required to hold a seller's permit by reason of the producer's sales of hay, regardless of whether the hay is sold for resale or at retail, and regardless of whether the hay sold at retail constitutes feed for any form of animal life of a kind the products of which ordinarily constitute food for human consumption, unless, operative April 1, 1996, the producer is a grower who produces hay for sale only to beef cattle feedlots or dairies or is a grower who sells exclusively through a farmer-owned cooperative.</p> <p>However, an occasional sale includes a sale of property by a producer of hay, other than hay, provided that the sale is not one of a series of sales sufficient in number, scope, or character to constitute an activity for which the producer would be required to hold a seller's permit if the producer were not also selling hay.</p> <p>The producer's sale of tangible personal property held or used in the course of an activity of producing the hay (such as farm equipment and machinery) is an occasional sale, provided all of the following conditions apply:</p>	<p>(d) MANUFACTURERS AND WHOLESALERS. A manufacturer, wholesaler, or other person in the business of making sales for resale of tangible personal property of a kind the retail sale of which is taxable whether or not the property is ever sold at retail or is suitable for sale at retail, is liable for tax measured by receipts from any of the person's retail sales of tangible personal property.</p> <p>(e) PRODUCERS OF HAY. A producer of hay is required to hold a seller's permit by reason of the producer's sales of hay, regardless of whether the hay is sold for resale or at retail, and regardless of whether the hay sold at retail constitutes feed for any form of animal life of a kind the products of which ordinarily constitute food for human consumption, unless, operative April 1, 1996, the producer is a grower who produces hay for sale only to beef cattle feedlots or dairies or is a grower who sells exclusively through a farmer-owned cooperative.</p> <p>However, an occasional sale includes a sale of property by a producer of hay, other than hay, provided that the sale is not one of a series of sales sufficient in number, scope, or character to constitute an activity for which the producer would be required to hold a seller's permit if the producer were not also selling hay.</p> <p>The producer's sale of tangible personal property held or used in the course of an activity of producing the hay (such as farm equipment and machinery) is an occasional sale, provided all of the following conditions apply:</p>	

**Proposed Regulatory Changes to Clarify the Application of Tax to Sales Requiring a  
Seller's Permit (Regulation 1595)  
Comparison of Current and Proposed Language**

Current as of July 12, 2000

Action Item	Current Regulatory Language	Regulatory Language Proposed by Staff	Summary Comments
	<p>(1) The sale is not one of three or more sales of tangible personal property (other than hay) for substantial amounts in any period of 12 months.</p> <p>(2) The sale is not one of a substantial number of sales of tangible personal property (other than hay) for relatively small amounts in any period of 12 months.</p> <p>(3) The tangible personal property was not also held or used in the course of an activity (other than the production of hay) for which a seller's permit is required, or would be required if the activity were conducted in this state.</p>	<p>(1) The sale is not one of three or more sales of tangible personal property (other than hay) for substantial amounts in any period of 12 months.</p> <p>(2) The sale is not one of a substantial number of sales of tangible personal property (other than hay) for relatively small amounts in any period of 12 months.</p> <p>(3) The tangible personal property was not also held or used in the course of an activity (other than the production of hay) for which a seller's permit is required, or would be required if the activity were conducted in this state.</p>	

**Regulation 1595. Occasional Sales--Sale of a Business--Business Reorganization.****(a) ACTIVITIES REQUIRING SELLER'S PERMIT.**

(1) GENERAL. Tax applies to all retail sales of tangible personal property including capital assets whether sold in one transaction or in a series of sales, held or used by the seller in the course of an activity or activities for which a seller's permit or permits is required or would be required if the activity or activities were conducted in this state. See subdivision (e) below for special rules regarding sales of property by producers of hay.

Generally, a person who makes three or more sales for substantial amounts in a period of 12 months is required to hold a seller's permit regardless of whether the sales are at retail or are for resale. Each sale of the person during the 12 month period is included in determining whether that person is required to hold a permit, or would be required to hold a permit if the activities were conducted entirely inside this state. Thus, a sale occurring outside California, whether at retail or for resale, is included, even though it would not be subject to California sales tax. A person who makes a substantial number of sales for relatively small amounts is also required to hold a seller's permit.

Tax does not apply to a sale of property held or used in the course of an activity not requiring the holding of a seller's permit unless the sale is one of a series of sales sufficient in number, scope and character to constitute an activity for which the seller is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state. If tangible personal property is leased under a lease which is a "sale" as defined in Revenue and Taxation Code Section 6006 or a "purchase" as defined in Revenue and Taxation Code Section 6010, tax applies to the lease as provided in Regulation 1660 (18 CCR 1660), and the lessor must hold a seller's permit as provided in Regulation 1699 (18 CCR 1699). The lessor is not making an occasional sale since the lessor is making a "continuing sale" and is thereby holding the leased property in an activity requiring the holding of a seller's permit. As such, the lessor's sale of the leased property at the end of the lease term is likewise not an occasional sale.

(2) PROPERTY HELD OR USED IN AN ACTIVITY, OR ACTIVITIES REQUIRING THE HOLDING OF A SELLER'S PERMIT. A seller's permit is required of a person engaged in the business of selling tangible personal property. An activity requiring the holding of that permit includes, but is not limited to, the acquisition and sale of tangible personal property, whether the person's sales are all at retail, all for resale, or include both sales at retail and sales for resale.

Acquisition includes the obtaining of the property in any manner whatsoever. For example, raw materials may be purchased or may be obtained by extraction from the earth, air or waters of the earth. These may be sold in raw form or processed or manufactured into other raw materials, component parts or finished items which are sold. Each of these activities is

an activity which is so related to the sale of tangible personal property, that it is part of the activity requiring the holding of a seller's permit.

(3) **SEPARATE BUSINESSES.** A person engaged in an activity or activities requiring the holding of a seller's permit or permits may also be engaged in entirely separate endeavors which do not require the holding of a seller's permit or permits. Tax applies to the sale of tangible personal property held or used in the course of an activity requiring the holding of a seller's permit. Tax does not apply to the sale of property held or used by the seller in the non-selling endeavors which do not require the holding of a permit unless that sale is itself one of a series of sales requiring the holding of a seller's permit. For example, a person may own a hardware store at one location and a real estate brokerage business at another location, with no relationship between the two activities except that of common ownership. Under these circumstances, a sale of furniture used in the brokerage business would not be a sale of property held or used in an activity requiring the holding of a seller's permit unless it was one of a series of sales of the property of the brokerage business. A sale of tangible personal property held or used in the hardware business would be a sale of property held or used in an activity requiring the holding of a seller's permit.

(4) **SERIES OF SALES REQUIRING THE HOLDING OF A SELLER'S PERMIT.** ~~When a~~ A person not otherwise engaged in an activity requiring the holding of a seller's permit may make ~~makes~~ a series of sales sufficient in number, scope and character to require the holding of a seller's permit, ~~the gross receipts from all of such sales are subject to tax.~~ The sale in that series of sales, and subsequent sales, during any 12 month period which resulted in the requirement to hold a permit are subject to tax, unless otherwise exempt.

**(A) Number.**

1. Generally the minimum number of sales to require the holding of a seller's permit by a person not otherwise engaged in a selling activity is three within any 12 month period.

2. When calculating the minimum number of sales which requires a person to hold a seller's permit, the following types of sales are excluded:

- a. Sales made by an auctioneer on behalf of the person. In such transactions, the auctioneer is the retailer liable for tax.
- b. Sales through claiming races of horses owned by the person. In such transactions, the racing association is the retailer liable for tax.
- c. Sales of vehicles, mobilehomes, commercial coaches, vessels, or aircraft which are exempted from sales tax by Revenue and Taxation Code Sections 6282 and 6283.
- d. A trade-in made by the person which is incidental to a nonselling activity of the person.

**(B) Scope.** The extent of the sales measured by their frequency or dollar volume.

**(C) Character.** This relates to the similarity in type and value giving effect to the taxpayer's operations. For example, a processor of food products for human consumption is

not required to hold a seller's permit for the processing and sale of food products. Sales of used lug boxes, obsolete or used machinery, food handling and similar items are of a character that three or more sales of sufficient scope will require the processor to hold a seller's permit for this selling activity.

(5) EXAMPLES APPLYING THE ABOVE PRINCIPLES.

(A) Service enterprises which make some incidental sales.

1. Operators of service enterprises such as hospitals, hotels, theaters, schools, laundromats, car washes, transportation companies, and trucking companies may make some sales incidental to their primary service business. A hospital may operate a pharmacy and cafeteria as an adjunct to the hospital. A hotel may operate a restaurant and a bar. A theater may sell popcorn to patrons. A school may operate a cafeteria and bookstore. A laundromat may sell soap to its customers.

If any of these businesses were sold, tax would apply only to the gross receipts from the tangible personal property held or used in the selling activity.

2. If, in any 12 month period, the operator of the service enterprise makes more than two sales in substantial amounts of tangible personal property used in the service enterprise, ~~none of the sales qualify as an occasional sale~~ the first two sales are exempt occasional sales, but the operator is required to hold a permit for the third and subsequent sales during any 12 month period. The gross receipts from the third and subsequent sales during any such 12 month period are subject to tax, unless otherwise exempt. For example, if one sale is a sale in interstate commerce, the gross receipts from that sale would be exempt; however, the gross receipts from the other sales would be taxable. If one of the sales is a sale of the business, sales tax applies to the gross receipts from the retail sale of the tangible personal property located in California and use tax applies to the sales price of property purchased for use in California and used in this state. For example, the only sales that a service enterprise made were the following sales (each of which was "substantial" for purposes of this regulation) of tangible personal property used in the service enterprise:

a. February 23, 1996	Occasional sale
b. August 16, 1996	Occasional sale
c. January 8, 1997	Not occasional sale
d. February 8, 1997	Not occasional sale
e. January 27, 1998	Occasional sale
f. February 3, 1998	Not occasional sale
g. August 11, 1999	Occasional sale
h. December 12, 1999	Occasional sale
i. September 8, 2000	Occasional sale
j. December 9, 2000	Not occasional sale

Sales a. and b. are occasional sales since since they were the first two sales made by the service enterprise.

Sales c. and d. are not occasional sales since they were the third and fourth sales in the series of sales commencing on February 23, 1996, which was less than 12 months prior to these sales.

Sale e. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on February 8, 1997. The January 8, 1997 sale is not relevant since it occurred more than 12 months prior to sale e.

Sale f. is not an occasional sale since it was the third sale in the series of sales commencing on February 8, 1997, which was less than 12 months prior to this sale.

Sale g. is an occasional sale since the service enterprise made no other sales in the prior 12 months.

Sale h. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on August 11, 1999.

Sale i. is an occasional sale since it was only the second sale in the series of sales commencing within the prior 12 months, on December 12, 1999.

Sale j. is not an occasional sale since it was the third sale in the series of sales commencing within the prior 12 months, on December 12, 1999.

**(B) Other businesses.**

1. Tax applies to the sales of assets of a business which is not essentially a service enterprise. Examples of this are sales of grocery stores and liquor stores making both exempt sales of food products for human consumption and taxable sales of other tangible personal property, service stations which sell gasoline, oil and similar items and which also perform automotive repairs and lubrication services, and computer stores which also provide training in the use of computers and repairs for computer products.

2. Where a service enterprise and a sales business are operated together so as to constitute one business, tax will apply to the sale of the assets of the business. For example, if a car wash and gasoline station are operated at the same premises and the car wash is available only to persons who buy gasoline or if the price of the car wash is reduced if gasoline is purchased, tax applies to the sale of the car wash.

3. A person purchases a hardware store with the intent of selling tangible personal property. The person must hold a seller's permit regardless of the number of sales of tangible personal property actually made. For example, if the person makes only two sales, a sale of a hammer and a sale of the business, neither sale is an occasional sale.

4. A person intends to create and sell custom furniture. The person must hold a seller's permit for all his or her sales of furniture. This is true even if, because of the time necessary to create each piece of furniture and the profit resulting from each sale, the person averages one sale of furniture per year.

(6) TRANSFER OF SHARES IN A CORPORATION. The sale of stock of a corporation is not a sale of tangible personal property and is not subject to sales tax. A stock purchase is not a purchase of tangible personal property and is not subject to sales or use tax notwithstanding the fact that the stock purchase may be treated as an asset acquisition for federal income tax purposes pursuant to Internal Revenue Code Section 338.

**(b) SALE OR REORGANIZATION OF ALL OR PART OF A BUSINESS.**

(1) GENERAL. In general, when a person sells a business which is required to hold a seller's permit, tax applies to the gross receipts from the retail sale of tangible personal property held or used by that business in the course of its activities requiring the holding of the seller's permit. The gross receipts from the sale of the business include all consideration received by the transferor, including cash, notes, and any other property as well as any indebtedness assumed by the transferee. It is irrelevant that the indebtedness assumed may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. That is, the transferor is selling a business, and all consideration received is for that business. The measure of tax is the price agreed to by the parties. In the absence of an agreement as to the price of the tangible personal property, the gross receipts from that sale is allocated among the taxable portion and the nontaxable portion by dividing the selling price of the tangible personal property acquired by the purchaser for use rather than resale by the selling price of the entire business sold, and then multiplying that amount by the total gross receipts (i.e., all consideration) received for the business. Book value will be regarded as establishing the price of properties sold. (See Regulation 1610 for special rules applicable to sales of vehicles, vessels, and aircraft.)

(2) TRANSFERS OF SUBSTANTIALLY ALL PROPERTY WITHOUT SUBSTANTIAL CHANGE IN OWNERSHIP. Tax does not apply to a transfer of all or substantially all the property held or used by a person in the course of activities for which the person is required to hold a seller's permit or permits or would be required to hold a seller's permit or permits if the activities were conducted in this state, provided that after the transfer the real or ultimate ownership of the property is substantially similar to that which existed before such transfer. "Substantially all the property" means 80 percent or more of all the tangible personal property held or used by the person in the course of activities requiring the holding of a seller's permit, including tangible personal property located outside of this state. If a person engages in two or more separate selling activities, for each of which the person is required to hold a seller's permit or would be required to hold a seller's permit if the activity were conducted in this state, a transfer of 80 percent or more of the tangible personal property held or used in the combined activities must be made in order to qualify

for the exemption described in this paragraph. If a person simultaneously transfers all or substantially all of its assets to more than one entity, the transfer will qualify for the exemption if the ownership remains substantially similar. Stockholders, bondholders, partners, or other persons holding an ownership interest rather than a security interest in the corporation or other entity are regarded as having the real or ultimate ownership of the property of the corporation or other entity.

The real or ultimate ownership is “substantially similar” to that which existed before a transfer if 80 percent or more of that ownership of the tangible personal property is unchanged after the transfer. In the following example, the ownership is “substantially similar” to that which existed before the transfer:

Stock- holders	Interests in Transferor Corporation	Interests in Transferee Corporation	Interests Common Before and After Transfer
A	40%	33 1/3%	33 1/3%
B	40%	33 1/3%	33 1/3%
C	20%	33 1/3%	20%
	100%	100%	86 2/3%

(3) **STATUTORY MERGER.** A transfer pursuant to a statutory merger is not a sale but is instead a transfer by operation of law. Thus, tax does not apply to a transfer of property of a constituent corporation to a surviving corporation or new corporation pursuant to a statutory merger under Sections 6010-6022, 1100-1305, or 15678.1-15678.9 of the California Corporations Code or similar laws of this state or other states. The surviving corporation stands in the place of each constituent corporation (including the disappearing corporation(s)). As a result, if property acquired by the surviving corporation in the merger had been purchased and held by the constituent corporation for resale, then the surviving corporation must report and pay use tax on the constituent corporation's purchase price if it makes any use of such resale property, just as the constituent corporation would have owed such tax if it had used the property. Similarly, if the constituent corporation had avoided paying tax measured by the purchase price of mobile transportation equipment by making a timely election to report tax on the fair rental value, the surviving corporation must continue to report tax measured by the fair rental value on its leases of the mobile transportation equipment; if the surviving corporation makes any use of that mobile transportation equipment other than leasing it to another person, the surviving corporation must report tax on the purchase price paid by the constituent corporation.

(4) **CONTRIBUTION TO COMMENCING CORPORATION, LIMITED LIABILITY COMPANY, PARTNERSHIP, OR JOINT VENTURE.** The transfer of tangible personal property to a commencing corporation, commencing limited liability company, commencing partnership, or commencing joint venture in exchange solely for first issue stock of the commencing corporation or an interest in the commencing limited liability company, partnership, or joint venture is not a sale since the interest received by the



transferor is not regarded as having measurable value at the time of the transfer. The transferor is the consumer of such property. However, such a transfer is a sale if the transferor receives any consideration, such as cash, notes, or an assumption of indebtedness (whether or not the transferor retains any joint liability with respect to the indebtedness assumed by the transferee), and tax applies to that sale unless it otherwise qualifies for exemption. For purposes of determining the measure of tax from the sale, it is irrelevant that any of the transferor's indebtedness assumed by the transferee may have arisen solely in connection with the transferor's acquisition of the tangible personal property transferred, the other property transferred, or some combination thereof. The gross receipts from that sale is allocated among the taxable portion and the nontaxable portion by dividing the selling price of the tangible personal property transferred to the purchaser for use rather than for resale by the selling price of all property transferred and then multiplying that amount by the total gross receipts (i.e., all consideration) received by the transferor.

When the transferor is a consumer under the previous paragraph, no tax applies with respect to the transfer provided the transferor's use of the property in California would not otherwise be subject to tax. For example, in the case of property purchased by the transferor for resale without payment of the tax, the transferor is the consumer of such property which the transferee will not sell. Since the transferor's use of such resale inventory is subject to tax, the transferor owes tax measured by its purchase price. However, no tax applies with respect to the transfer of such resale inventory provided the transferee will sell such property without any use other than retention, demonstration, and display while holding the property for sale. If the transferee thereafter makes any other use of such property, it must report use tax measured by the transferor's purchase price.

(5) **DISSOLUTION OF CORPORATION.** A distribution of assets, including tangible personal property, by a corporation upon its dissolution to its stockholders in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the corporation other than the stockholders' return of stock certificates for purposes of cancellation. The corporation is the consumer of such property and no tax applies with respect to the transfer provided the corporation's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the stockholders, tax applies measured by that consideration.

(6) **DISSOLUTION OF LIMITED LIABILITY COMPANY.** A distribution of assets, including tangible personal property, by a limited liability company upon its dissolution to its members (i.e., persons holding membership interests and persons holding economic interests) in accordance with their ownership interests is a liquidating dividend and is not a sale when no consideration is received by the limited liability company other than cancellation of the members' interests. The limited liability company is the consumer of such property and no tax applies with respect to the transfer provided the limited liability company's use of the property in California would not otherwise be subject to tax. If consideration is given or received for the transfer, such as an assumption of liabilities by the members, tax applies measured by that consideration.

(7) **DISSOLUTION OF PARTNERSHIP.** A partnership is a person for sales and use tax purposes. (Revenue and Taxation Code Section 6005.) However, a partnership is defined for general law purposes as an association of two or more persons to carry on as co-owners a business for profit. (Corporations Code Section 15006.) Dissolution of a partnership is caused by withdrawal of a partner or admission of a new partner, unless otherwise provided in an agreement in writing signed by all the partners, including any such withdrawing partner or any such newly admitted partner before such withdrawal or admission. (Corporations Code Section 15031(7).)

Under Corporations Code Section 15026, a partner's interest in the partnership is the partner's share of the profits and surplus, and is personal property. Under Corporations Code Section 15027(1), a conveyance by a partner of that partner's interest in the partnership does not in itself dissolve the partnership, nor, as against the other partners in the absence of agreement, entitle the assignee, during the continuance of the partnership, to interfere in the management or administration of the partnership business or affairs, or to require any information or account of partnership transactions, or to inspect the partnership books; but it merely entitles the assignee to receive in accordance with the partnership contract the profits to which the assigning partner would otherwise be entitled. The assignment of a partnership interest in this technical sense is not a sale of tangible personal property and is not subject to tax.

In common usage, however, the term "partnership interest" refers to all of the rights of a partner including (1) the person's rights in specific partnership property, (2) the person's interest (in the technical sense) in the partnership, and (3) the person's right to participate in the management. In a typical commercial transaction when a partner "sells the person's interest in a partnership" to another, it is intended that the person "selling the interest" will withdraw from the partnership and the person "purchasing the interest" will be admitted to the partnership. The legal effect of this transaction is to dissolve the first partnership and to create a new partnership, in the absence of a provision in the agreement providing for continued life of the partnership. The effect for sales and use tax purposes is that there is a dissolution of the partnership, a distribution of the assets on a pro rata basis, and a sale by the withdrawing partner of the person's ownership interest in the tangible personal property distributed to that person. Except as provided in subdivision (c), this sale of tangible personal property will qualify as an occasional sale under Revenue and Taxation Code Section 6006.5 and will be nontaxable under Section 6367, unless the withdrawing partner holds a seller's permit or the sale of tangible personal property is one of a series of sales sufficient in number, scope, and character to require the holding of a seller's permit.

A distribution of assets, including tangible personal property, by a partnership upon its dissolution to the partners in accordance with their ownership interests in the partnership is a liquidating dividend and is not a sale when no consideration is received by the partnership other than cancellation of the partners' interests. The partnership is the consumer of such property and no tax applies with respect to the transfer provided the partnership's use of the property in California would not otherwise be subject to tax. If consideration is given or

received for the transfer, such as an assumption of liabilities by the partners, tax applies measured by that consideration.

Where a partnership distributes some of its assets in the form of a partial liquidation of the business, the transfer will be regarded as a liquidating dividend, subject to the rules set forth in the previous paragraph, if an entire segment of the business of the partnership is being liquidated. For example, a partnership operates a lumberyard and an automobile repair and parts business. If the partnership ceases operation of the lumberyard and distributes its assets to the partners in accordance with their interest in the partnership and the partnership receives no consideration from the partners such as an assumption of liabilities, the transfer is a liquidating dividend subject to the rules set forth in the previous paragraph. If, however, the partnership ceases operating the repair portion of the automobile repair and parts business and distributes the assets of that portion of the business, it is not liquidating an entire segment of its business and the transfer does not qualify as a nontaxable liquidating dividend.

(8) **DISSOLUTION OF JOINT VENTURE.** For purposes of this paragraph, a joint venture is an undertaking by two or more persons jointly to carry out a single enterprise for profit. The rules applicable to a partnership's liquidating dividends apply to a joint venture's liquidating dividends. The distribution of assets by a joint venture will be regarded as a liquidating dividend, subject to the rules set forth for partnerships, provided at least 80 percent of the purpose of the joint venture has been completed at the time of the distribution. The distribution of the assets of a joint venture prior to 80 percent completion of the purpose of the joint venture cannot qualify as a liquidating dividend and is a sale transaction subject to tax.

(9) **SALE FOLLOWING LIQUIDATION.** Except as provided in subdivision (c), the transferee's sale of assets acquired in a transfer qualifying as a liquidating dividend, as discussed in this regulation, would be an exempt occasional sale if the property is not sold as part of an activity requiring the holding of a seller's permit and is not one of a series of sales requiring the holding of a seller's permit.

**(c) VEHICLES, MOBILEHOMES, COMMERCIAL COACHES, VESSELS, AND AIRCRAFT.** There is no occasional sale exemption for the sale or use of vehicles required to be registered with the Department of Motor Vehicles, or off-highway vehicles subject to identification under Division 16.5 of the Vehicle Code, mobilehomes and commercial coaches required to be registered with the Department of Housing and Community Development, vessels, or aircraft, as defined by the law and in Regulation 1610 (18 CCR 1610) or in Regulation 1610.2 (18 CCR 1610.2), except when such property is included in a transfer of all or substantially all the property held or used in the course of business activities of the person selling the property and the real or ultimate ownership of the property is substantially similar to that which existed before such transfer. The rules set forth in subdivision (b)(2) of this regulation are applicable in determining under this paragraph whether a transfer is of substantially all the property and whether the ownership is substantially similar.

**(d) MANUFACTURERS AND WHOLESALERS.** A manufacturer, wholesaler, or other person in the business of making sales for resale of tangible personal property of a kind the retail sale of which is taxable whether or not the property is ever sold at retail or is suitable for sale at retail, is liable for tax measured by receipts from any of the person's retail sales of tangible personal property.

**(e) PRODUCERS OF HAY.** A producer of hay is required to hold a seller's permit by reason of the producer's sales of hay, regardless of whether the hay is sold for resale or at retail, and regardless of whether the hay sold at retail constitutes feed for any form of animal life of a kind the products of which ordinarily constitute food for human consumption, unless, operative April 1, 1996, the producer is a grower who produces hay for sale only to beef cattle feedlots or dairies or is a grower who sells exclusively through a farmer-owned cooperative.

However, an occasional sale includes a sale of property by a producer of hay, other than hay, provided that the sale is not one of a series of sales sufficient in number, scope, or character to constitute an activity for which the producer would be required to hold a seller's permit if the producer were not also selling hay.

The producer's sale of tangible personal property held or used in the course of an activity of producing the hay (such as farm equipment and machinery) is an occasional sale, provided all of the following conditions apply:

- (1) The sale is not one of three or more sales of tangible personal property (other than hay) for substantial amounts in any period of 12 months.
- (2) The sale is not one of a substantial number of sales of tangible personal property (other than hay) for relatively small amounts in any period of 12 months.
- (3) The tangible personal property was not also held or used in the course of an activity (other than the production of hay) for which a seller's permit is required, or would be required if the activity were conducted in this state.